ARBUTHNOT BANKING GROUP PLC

20 March 2014

For immediate release

ARBUTHNOT BANKING GROUP (“Arbuthnot”, “the Group” or “ABG”)
Audited Final Results for the year to 31 December, 2013

Significant Growth

Arbuthnot Banking Group today announces a 25 percent increase in profit before tax of £15.7m. Significant progress has been made across the Group during the year as we continue to realise our ambitions to grow.

Arbuthnot Banking Group PLC is the holding company for Arbuthnot Latham & Co., Limited and Secure Trust Bank PLC.

FINANCIAL HIGHLIGHTS

- Profit before tax £15.7m (2012: £12.6m)
- Underlying Profits of £18.6m (2012: £11.6m)
- Operating Income exceeded £100m for the first time (2012: £65.6m)
- Achieved positive operating leverage of 14%*
- Earnings per share 52p (2012: 53p)
- Total dividend per share 44p (2012: 25p) including a special dividend of 18p
- Total assets increased to £1.1bn (2012: £1.0bn)
- Net assets per share 570.5p (2012: 449.3p) an increase of 27%

OPERATIONAL HIGHLIGHTS

Private Banking - Arbuthnot Latham

- Profit before tax £7.7m (2012: £2.1m)
- Customer loans up 18% to £341.0m (2012: £289.3m)
- Customer deposits grew £24m to £519.7m (2012: £495.7m)
- Assets under Management increased 40% to £528m (2012: £377m)

Retail Banking - Secure Trust Bank

- Profit before tax £17.2m (2012: £17.3m) with underlying profits of £25m
- Acquired V12 loans adding £36.8m of customer loans
- Lending balances increased by 31% to £391.0m (2012: £297.6m)
- Total customer numbers increased to 350,861 (2012: 231,713)
- SME Lending commenced

Commenting on the results, Henry Angest, Chairman and Chief Executive of Arbuthnot, said: “This has been another significant year. Both banks have made good progress. We have substantially increased the net assets of the Group and at the same time been able to pay shareholders a special dividend.”

*Percentage difference between the increase in Operating Income and Operating Expenses

Note: Secure Trust Bank is also making its final results announcement today which should be read in conjunction with this statement.

ENQUIRIES:

Arbuthnot Banking Group
Henry Angest, Chairman and Chief Executive 020 7012 2400
Andrew Salmon, Chief Operating Officer
James Cobb, Group Finance Director
David Marshall, Director of Communications

Canaccord Genuity Ltd (Nominated Advisor)
Lawrence Guthrie 020 7665 4500
Sunil Duggal

Numis Securities Ltd (Broker)
Chris Wilkinson 020 7260 1000

ARBUTHNOT BANKING GROUP PLC

Mark Lander

Bell Pottinger (Financial PR)
Ben Woodford 020 7861 3917
Zoë Pocock

The 2013 Annual Report and Notice of Meeting will be posted and available on the Arbuthnot Banking Group website http://www.arbuthnotgroup.com on or before 7 April 2014. Copies may be obtained from the Company Secretary, Arbuthnot Banking Group PLC, Arbuthnot House, 20 Ropemaker Street, London, EC2Y 9AR.

Consolidated statement of comprehensive income

	Note	Year ended 31 December 2013 £000	Year ended 31 December 2012 £000
Interest income		93,329	62,300
Interest expense		(20,279)	(17,514)
Net interest income		**73,050**	**44,786**
Fee and commission income	8	31,816	24,116
Fee and commission expense		(4,846)	(3,347)
Net fee and commission income		**26,970**	**20,769**
Operating income		**100,020**	**65,555**
Net impairment loss on financial assets	9	(18,807)	(10,984)
Gain from a bargain purchase	10	413	9,830
Gain on sale of building	11	6,535	-
Gain on sale of subsidiary	12	-	839
Other income	13	1,183	396
Operating expenses	15	(73,631)	(53,043)
Profit before income tax from continuing operations		**15,713**	**12,593**
Income tax expense	17	(4,198)	(1,128)
Profit after income tax from continuing operations		11,515	11,465
Loss from discontinued operations after tax	14	-	(347)
Profit for the year		**11,515**	**11,118**
Other comprehensive income			
Items that are or may be reclassified to profit or loss			
Foreign currency translation reserve		-	570
Revaluation reserve			
Cash flow hedging reserve			
- Effective portion of changes in fair value		(15)	(34)
Available-for-sale reserve		(250)	81
Other comprehensive income for the period, net of tax		**(265)**	**617**
Total comprehensive income for the period		**11,250**	**11,735**
Profit attributable to:			
Equity holders of the Company		7,930	8,041
Non-controlling interests		3,585	3,077
Profit for the year		**11,515**	**11,118**
Total comprehensive income attributable to:			
Equity holders of the Company		7,681	8,658
Non-controlling interests		3,569	3,077
Total comprehensive income for the period		**11,250**	**11,735**

	Note		
Earnings per share for profit attributable to the equity holders of the Company during the year (expressed in pence per share):			
- basic and fully diluted	18	51.9	52.6

Consolidated statement of financial position

		At 31 December	
		2013	2012
	Note	£000	£000
ASSETS			
Cash	19	193,046	203,683
Loans and advances to banks	20	105,061	144,391
Debt securities held-to-maturity	21	19,466	13,526
Derivative financial instruments	22	508	648
Loans and advances to customers	23	732,009	586,968
Other assets	25	17,267	11,666
Financial investments	26	1,975	3,257
Deferred tax asset	27	3,954	5,057
Investment in associate	28	943	-
Intangible assets	29	13,103	8,326
Property, plant and equipment	30	5,522	22,487
Total assets		**1,092,854**	**1,000,009**
EQUITY AND LIABILITIES			
Equity attributable to owners of the parent			
Share capital	36	153	153
Retained earnings	37	67,901	53,372
Other reserves	37	(1,467)	(1,253)
Non-controlling interests		**20,327**	**16,376**
Total equity		**86,914**	**68,648**
LIABILITIES			
Deposits from banks	31	2,003	373
Derivative financial instruments	22	371	462
Deposits from customers	32	957,791	894,545
Current tax liability		1,427	346
Other liabilities	33	31,017	23,021
Deferred tax liability	27	1,099	634
Debt securities in issue	34	12,232	11,980
Total liabilities		**1,005,940**	**931,361**
Total equity and liabilities		**1,092,854**	**1,000,009**

Chairman’s statement

I am pleased to report that Arbuthnot Banking Group (“ABG” or “the Group”) has delivered a profit before tax of £15.7m (2012: £12.6m) which represents a 25% increase on 2012.

But more importantly, I note that both banks have been realising their ambitions for growth. It has always been a philosophy of the Group to build a varied source of income streams and to spread its risks, rather than become overly reliant or concentrated on a small number of business lines.

Notably, Secure Trust Bank (“STB”) continued its diversification, as it completed the acquisitions of V12 Finance Group and Debt Managers Ltd early in 2013. These were complementary to the purchase of Everyday Loans made in 2012. All of these businesses have been successfully integrated into the Group.

At the same time Arbuthnot Latham ("AL") opened for business in Dubai, agreed a client custody arrangement with Pictet one of the largest Private Banks in Geneva, that allows Arbuthnot Latham's clients to use their services in Switzerland, Singapore and Hong Kong, installed a new operating platform for its investment management business and grew its total customer account balances to £1.05bn (2012: £872.3m).

During the year the Group took further steps to underpin the long term growth potential of both businesses by completing two significant transactions. First, we entered into a sale and lease back agreement on the Group's new headquarters at 7-21 Wilson Street. Having purchased the freehold in August 2012 for £15.7m, we could not refuse an offer that produced a net profit of £6.5m only a year later. Secondly, the Group continued to provide more liquidity to the market, by selling 580,000 shares in STB on 13 December 2013. Although we are prevented from showing the transaction as a profit by those curious accounting rules, the gain on sale of £14.4m has further increased the financial strength of the Group. Such is this strength and confidence for the future, the Directors were able to declare a special dividend of 18 pence to mark the 180 year anniversary of Arbuthnot Latham.

In last year's Chairman's Statement, I made reference to the regulatory environment in which both our banks operate and how the rules create a "glass ceiling" which prevents small banks becoming true challengers. During this year I have been pleased to detect a change in sentiment. In October the Governor of the Bank of England announced that it was open for business and would play its part in helping the banking industry with the introduction of new liquidity support mechanisms. These would be made available to all banks and not just the large lenders, who were usually the only ones able to offer mainstream forms of collateral, that were previously required to participate. The Bank's view is now that as long as it could assess the credit risk of assets, they would be welcome as collateral.

This may seem like a small step forward, but to a well-managed banking Group such as ours, that has for years been excluded from such schemes, the news was welcome. We trust that the Bank of England truly understands the important role that the small banks can play in delivering an excellent service to its customers and also in helping to sustain the economic recovery.

During the year, Arbuthnot Latham celebrated its 180 year anniversary. I am proud of the history of our Private Bank, having been involved in shaping the City of London into one of the pre-eminent financial centres of the world. As part of the celebrations we published a book that recorded this history and I was particularly delighted that the Mayor of London, Boris Johnson, accepted our invitation to write the foreword to the book. He observed that despite its lack of natural resources, the City has built its success based on entrepreneurial spirit and free market forces.

I am, however, alarmed at the recent developments and rhetoric that have been aimed at restricting the free market. These have included wage control, caps on interest rates charged, limits on market share, regulating profitability, breaking up bank branch networks and raising the tax burden levied on the entrepreneurial classes and finally the threat of a financial transaction tax, all of which creates uncertainty for investors. This can only be unhelpful in maintaining the economic recovery, which is clearly underway.

Private Banking – Arbuthnot Latham & Co., Ltd

The Private Banking business has reported a pre-tax profit of £7.7m (2012: £2.1m). This result was clearly flattered by the gain of £6.5m that was generated from the sale and lease back transaction on the Wilson Street property. However, this should not overshadow the real progress that was made by Arbuthnot Latham during the year. As mentioned previously, we took the conscious decision to invest for the long term future. These investments are clearly coming to fruition when I reflect on the momentum that is being generated.

We have always held a long term ambition to develop our distribution capabilities to cover overseas markets. I feel we reached a major milestone this year, when we opened for business in Dubai. The predominately wealth management service appears to have been well received by the market in Dubai. The generation of new business there has exceeded our initial expectations. We have also added further options for our customers who wish to gain exposure to other overseas markets, via our custody arrangements with Pictet, which were initiated during the year.

In order to keep pace with the growing scale of our Investment Management business, the operating platform was replaced with new technology. This now offers the customers online facilities, which allows them immediately to review their portfolios. Early in 2014 we also launched our new mobile banking application as we continue to respond to the ever increasing needs of our clients.

Retail Banking – Secure Trust Bank PLC

The reported pre-tax profits of Secure Trust Bank were £17.2m (2012: £17.3m). However, once again the reported numbers do not tell the entire story of the progress being made by our retail bank. The underlying profits for STB were £25.2m, which is a record for the bank.

The business has maintained its focus on serving customers well and meeting their needs with simple straight forward banking solutions. This resulted in our customer numbers growing by 51% to close the year at 350,861 (2012: 231,713).

STB has continued to diversify its operations by adding to the acquisition of Everyday Loans in 2012 with further purchases this year of V12 Finance Group and Debt Managers Ltd. All these entities have been successfully integrated into the Group and the existing businesses have begun to leverage their expertise. The retail finance offering has been consolidated onto the V12 operating platform. Our personal loan portfolios are being managed as one business, to ensure we have an attractive offering to all our customers regardless of their standing. We have also transferred some of our existing impaired loans to Debt Managers Ltd to improve the financial returns involved in recovering these assets.

Board Changes and Personnel

The Board has remained unchanged throughout the year. I would like to take this opportunity to express my thanks to my colleagues on the Board for their generous support and the dedication they have given to the Group and me personally.

The results of the Group reflect the hard work and commitment of both existing and new members of staff who, with few exceptions, have performed well. On behalf of the Board I extend our thanks to all of them for their contributions in 2013.

Dividend

The Board is proposing a final dividend of 15p, an increase of 1p on last year, together with the interim dividend of 11p and the special dividend of 18p making a total dividend for the year of 44p (2012: 25p). If approved, the dividend will be paid on 16 May 2014 to shareholders on the register at close of business on 18 April 2014.

Outlook

With the economic recovery underway, both banks have worked hard to be in a position to prosper as the economy grows. We are therefore optimistic that we can continue to make good steady progress, while remaining focussed on the needs and aspirations of our customers. The outlook is bright, the economy is improving and business is prospering. This will last as long as politics does not interfere with it.

Strategic Report

Business Review - Private Banking - Arbuthnot Latham

	2013	2012
Operating income	£21.7m	£18.9m
Other income	£10.3m	£3.1m
Operating expenses	£21.3m	£17.9m
Profit before tax	£7.7m	£2.1m
Customer loans	£341.0m	£289.3m
Customer deposits	£521.2m	£495.7m
Total assets	£619.7m	£568.6m
Customer net margin	4.4%	3.3%
Loan to deposit ratio	66%	59%

Arbuthnot Latham celebrated its 180th anniversary in 2013 and during the year made good progress across many areas of business. The core business of private banking and wealth management, grew all key components of its business during the year and finished with a strong underlying momentum. The first international office for Arbuthnot Latham was opened in Dubai and through the establishment of international custody arrangements with Pictet, the Bank is now able to offer its services to wealthy clients from overseas who wish to have a private banking relationship in London. In addition, the sale and leaseback arrangement concluded for our new headquarters building produced a profit of £6.5m.

The year-end reported profit for Arbuthnot Latham was £7.7m with the core private banking and wealth management business delivering a profit of £4.9m (2012: £3.5m) before credit provisions.

The strategy to grow the private banking and wealth management business through the addition of several experienced bankers and the overall strengthening of the client proposition began to produce positive results during the year. With the recent upheaval across the financial services industry caused by the financial crisis, there is a significant opportunity for a client focused bank such as Arbuthnot Latham to benefit from clients looking to establish a new financial relationship.

This growth in new clients was reflected in the financial results. Client deposits ended the year at £521.2m (2012: £495.7m), an increase of 5%. The Bank was also able to draw on the Funding for Lending Scheme and by the year end had drawn £40m under this scheme. The overall cost of deposits fell during the year thereby enhancing the net interest income position of the Bank.
The loan book grew in 2013 by 18% to end the year at £341.0m (2012: £289.3m). The Bank continued its focus towards supporting the objectives of the client base with good quality lending transactions. The loan to deposit ratio at the end of the year was 66% (2012: 59%) which continued to reflect our prudent approach to the management of our balance sheet.

In the wealth management business, the strengthening of the client proposition and the attraction to clients of the independent approach of the Bank in its investment management services resulted in a 40% increase in assets under management which finished the year at £527.9m (2012: £376.6m).

Following the strategic decision to open an office in Dubai, the Bank received its licence to operate in the Dubai International Financial Centre from the Dubai Financial Services Authority in late July 2013. The business in Dubai is focused towards international private banking and wealth management services. Since opening the office, an encouraging and positive foundation has been established with several new accounts opened and the business is proceeding to plan. Dubai is a growing market for international financial services and Arbuthnot Latham is now well placed to share in the growth that this market is expected to experience over the next few years.

Our structured product distribution business, Gilliat Financial Solutions, experienced a challenging year with resulting weaker income margins across the business. While the UK distribution base continued to grow and the offshore business established some very positive distribution relationships, the business made a loss for the year of £0.4m (2012: £0.6m profit). The business has undertaken a review of its activities and we are confident that 2014 will see a return to profit.

Business Review - Retail Banking - Secure Trust Bank

	2013	2012
Operating income	£79.0m	£47.0m
Operating expenses	£46.7m	£30.7m
Profit before tax	£17.2m	£17.3m
Customer loans - unsecured	£391.0m	£297.6m
Customer deposits	£436.6m	£398.9m
Customer numbers	350,861	231,713
Net interest margin	16.9%	15.0%
Cost income ratio	0.55	0.59

Secure Trust Bank ("STB") has reported pre-tax profits of £17.2m (2012: £17.3m). The fact that the reported number is largely unchanged from the previous year does not reflect the true growth in profitability that is being generated by the bank. Shareholders will recall that the 2012 statutory profit included a fair value adjustment arising from the acquisition of Everyday Loans. The underlying profit of STB for 2013 is £25.2m, which represents a 51% increase on the prior year underlying profit of £16.8m. It should also be noted that since the IPO in November 2011, the bank's underlying profit before tax has increased by 220% from £7.9m.

Ultimately the success of the business will depend on the ability of STB to attract and serve its customers. During 2013 its strategy of providing simple and straight forward banking solutions has proved successful, as the number of customers grew by 51% to close the year at 350,861. This figure also represents a 142% increase since the flotation on the AIM market. As the opportunity to provide credit solutions remains attractive, given the reduced level of funding available from the high street banks, the lending operations of the bank have become the engine for growth in recent times. Once again this was the case in 2013.

Overall, new business lending volumes grew by 50% to £304.7m (2012: £202.5m). In turn, this resulted in an increase of 31% in total customer loans at £391m (2012: £297.6m). The Motor finance business, which focusses on the near prime market segments, continues to service the majority of the top 100 UK car dealer groups. The growth in the portfolio for the year was 28%, as balances closed at £114.6m (2012: £89.6m).

The personal unsecured loan portfolio increased by 14% to £77.9m (2012: £68.2m). The rate of growth in this portfolio was partly constrained by a significant delay in the commencement of a new bank to bank loan referral arrangement. This activity is now operational with Sainsbury's Bank and should deliver benefits in 2014.

This year saw STB take a significant step forward in developing its retail point of sale business. The growth in balances was as a result of strong demand from retailers and also the acquisition of V12 Finance. Accordingly, the customer balances grew by 78% to close the year at £114.4m (2012: £64.2m). The business made good progress in integration, creating a single retail finance offering. The

existing STB relationships have been transferred to the V12 platform. This has allowed the bank to offer a compelling proposition and has led to greater success in attracting retailers, notably including the recently announced Halfords agreement.

Everyday Loans portfolio grew to £81.4m (2012: £73.8m). This branch based unsecured lending portfolio serves relatively high credit risk customers with low average balance (£2,700) accounts. Given the higher risk in this business, the strategy has been to grow the portfolio in a controlled fashion, concentrating on profit maximisation rather than simply growth in volumes.

Once again the overall growth in the bank's lending portfolios has resulted in a higher level in the value of reported impairments. Given our prudent underwriting criteria, the actual rate of impairments remains lower than the level anticipated at origination and therefore below the rates at which the loans were priced.

The robust growth in the customer loan portfolios has continued to be matched by customer deposits. The balance sheet remains entirely funded by retail deposits with the year end loan to deposit ratio being 90%. However, as the markets begin to signal an eventual rise in interest rates, the profile of the average tenor of the bank's deposits has been extended. Fixed term deposits now represent 44% of the total deposit book, compared to 39% in the prior year.

Finally, to initiate the next phase of growth, the bank is in the process of entering the SME lending markets. The bank has already written a number of good quality real estate finance transactions and is exploring asset based finance opportunities. All of these are expected to develop further in 2014.

Strategic Report - Financial Review

Arbuthnot Banking Group PLC adopts a pragmatic approach to risk taking and seeks to maximise long term revenues and returns. Given its relative size, it is able to remain entrepreneurial and capable of taking advantage of favourable market opportunities when they arise.

The Group provides a range of financial services to customers and clients in its chosen markets of Private Banking (Arbuthnot Latham & Co., Limited) and Retail Banking (Secure Trust Bank PLC). The Group's revenues are derived from a combination of net interest income from lending, deposit-taking and money market activities, fees for services provided to customers and clients and commission earned on the sale of financial instruments and products.

Highlights

Summarised Income Statement	2013 £000	2012 £000
Net interest income	73,050	44,786
Net fee and commission income	26,970	20,769
Operating income	100,020	65,555
Gain from a bargain purchase	413	9,830
Gain from sale of building	6,535	-
Other income	1,183	396
Gain on sale of subsidiary	-	839
Operating expenses	(73,631)	(53,043)
Impairment losses - financial investments	(1,073)	-
Impairment losses - loans and advances to customers	(17,734)	(10,984)
Profit on continuing operations before tax	15,713	12,593
Income tax	(4,198)	(1,128)
Profit on continuing operations after tax	11,515	11,465
Loss from discontinued operations after tax	-	(347)
Profit after tax	**11,515**	**11,118**
Basic earnings per share (pence)	51.9	52.6

Underlying profit reconciliation 31 December 2013	Arbuthnot Latham & Co. £000	Secure Trust Bank £000	Arbuthnot Banking Group £000
Profit after tax	7,728	17,193	15,713
Gain on sale of building	(6,535)	-	(6,535)
180th Year anniversary	-	-	436

Dubai office investment	879	-	879
ELL fair value amortisation	-	4,066	4,066
STB acquisition costs	-	854	854
STB share options	-	2,221	2,221
V12 fair value amortisation	-	893	893
Acquired portfolios	-	1	1
Underlying profit	**2,072**	**25,228**	**18,528**
Basic earnings per share (pence)			40.6

Underlying profit reconciliation	Arbuthnot Latham & Co.	Secure Trust Bank	Arbuthnot Banking Group
31 December 2012	£000	£000	£000
Profit after tax	2,058	17,253	12,593
Bargain purchase gain on acquisition of ELL	-	(9,830)	(9,830)
ELL fair value amortisation	-	3,056	3,056
ELL management incentives	-	1,700	1,700
Excess funding costs of acquisition	-	1,900	1,900
STB acquisition costs	-	1,428	1,428
STB share options	-	1,610	1,610
Acquired portfolios	-	(363)	(363)
Gain on sale of Switzerland subsidiary	-	-	(839)
AL hire of new executives	300	-	300
Underlying profit	**2,358**	**16,754**	**11,555**
Basic earnings per share (pence)			38.2

Once again the Group has continued to trade robustly in 2013 and has reported a profit before tax of £15.7m (2012: £12.6m), which on a statutory basis represents an increase of 25%. However, the financial results for 2013 and those of 2012 contain a number of individually significant items. The Annual Report and Accounts for 2012 detail the bargain purchase gain that arose from the acquisition of Everyday Loans. This year the Group has recognised a £6.5m gain from the sale and lease back of the new head office building. Once the impact of these and a small number of other non-recurring items such as the recognition of the 180 year anniversary (£0.4m) are excluded from the results, the Group has underlying earnings of £18.5m (2012: £11.6m) which represents an increase in excess of 60%. Similarly, the statutory Earnings Per Share ("EPS") is 51.9 pence (2012: 52.6 pence), but the underlying EPS has increased by 6% to 40.6 pence (2012: 38.2 pence).

The Operating Income for the Group has exceeded £100m for the first time in the Group's history increasing by 53% as the full year impact of the acquisitions and the strong organic growth have emerged in the financial results. The largest component of the operating income remains Net Interest Income, which is now 73% of the total income. The approximate blended yield of Net Interest Income compared to average customer loans has increased to 11% against the prior year 9%. This is mainly as a result of the increasing proportion that Secure Trust Bank's higher yielding loan portfolios represent of the Group's asset base. Net Interest Income has also benefitted from lower deposit rates prevalent in the market, which has been brought about by the introduction of the Funding for Lending Scheme ("FLS").

The overall expense base increased to £73.6m (2012: £53m), which is an increase of 39%. Once again, the increase is mainly due to the full year impact of acquisitions and the cost of investment for growth. Relative to the growth in operating income, the Group has produced a positive operating leverage of 14%.

As expected, given the growth in the Group's lending portfolios, the impairment costs have increased by 60% in total. However, the total impairment charge compared to the total customer loan portfolio has held steady at a blended rate of below three percent (2013: 2.6%, 2012: 2.2%).

The Group tax charge has returned to a more normal level in 2013 following the significantly reduced amount of 2012 which was caused by the impact the bargain purchase gain had on the overall tax rate.

Balance Sheet Strength

	2013	2012

Summarised Balance Sheet	£000	£000
Assets		
Loans and advances to customers	732,009	586,968
Liquid assets	317,573	361,600
Other assets	42,905	51,441
Total assets	**1,092,487**	**1,000,009**
Liabilities		
Customer deposits	957,791	894,545
Other liabilities	47,782	36,816
Total liabilities	1,005,573	931,361
Equity	86,914	68,648
Total equity and liabilities	**1,092,487**	**1,000,009**

In the previous year the Group's total assets exceeded £1bn for the first time in its history. Once again the Group delivered strong growth in its total assets posting an increase of 9%. This was despite the fact that the level of liquid assets reduced by 13% in the year. The assets growth was as a result of the performance of the lending portfolios. In aggregate, customer loans increased by 25% to £732.2m (2012: £587m). The acquisition of V12 Finance contributed £36.8m.

The Group's lending remains entirely funded by customer deposits, which increased by 7% to £957.8m (2012: £894.5m). As a result, the overall loan to deposit ratio closed the year at 76.4% (2012: 65.5%). This increase was largely planned as both the Group's banks have been admitted into the Funding for Lending Scheme, which has provided access to a valuable source of new liquidity.

Also, shareholders should note that the net assets of the Group increased by £18.2m (27%) even after the payment of the special dividend. Contributing to this increase was not only the record earnings, but also the gain that arose on the sale by the Group of 580,000 shares in STB. This generated a non taxable gain of £14.4m that is required to be accounted for in the Statement of Changes in Equity. The net asset value per share of the Group is now 570.5p (2012: 449.3p).

Segmental Analysis

The segmental analysis in note 43 to the Consolidated Financial Statements of the Annual Report highlights the disclosures required under IFRS 8 'Operating Segments'. The operating segments are Private Banking (Arbuthnot Latham & Co., Limited) and Retail Banking (Secure Trust Bank PLC). Group costs and intercompany elimination journals are shown separately to reconcile back to the Group consolidated result.

The analysis presented below, and in the business review, is before any consolidation adjustments to reverse the impact of intergroup operating activities and also intergroup recharges and is a fair reflection of the way the Directors manage the Group.

Private Banking - Arbuthnot Latham

Summarised Income Statement	2013 £000	2012 £000
Net interest income	12,778	10,708
Net fee and commission income	8,873	8,187
Operating income	21,651	18,895
Gain from sale of building	6,535	-
Other income	3,765	3,072
Operating expenses	(21,309)	(17,871)
Impairment losses - financial investments	(824)	-
Impairment losses - loans and advances to customers	(2,090)	(2,038)
Profit before tax	**7,728**	**2,058**

The profit before tax increased to £7.7m (2012: £2.1m). However, as previously discussed, the results of the bank include the gain that arose on the sale of the Wilson Street property, which generated £6.5m. Also, as part of the year end analysis, the business took a more pessimistic view on its small number of equity investments that have been held in its Available-for-Sale portfolio. This resulted in incremental losses of £0.8m. The remaining equity investment portfolio now totals £1.8m.

As indicated to the market throughout 2013, the bank benefitted from a 20% increase in Net Interest Income, which was as a result of not only a larger customer asset portfolio but also a widening of customer margins of over 100 basis points. This was brought about by the impact of FLS on the market for deposit rates.

The investment made in the upgrade of the private banking front office began to pay off, resulting in growth in the assets under management of 40%. Accordingly, the bank saw an increase in the fees and commissions earned of 7%.

With greater confidence that the business model has sustainable momentum, further investments were made, not only in the front office but also the Dubai office which officially opened midway through the year. Additionally, a new investment management operating platform came online in the year, all of which resulted in an increase in operating expenses of 19%.

The credit losses declined to £1.8m (2012: £2.0m) which, on a larger portfolio, saw the actual loss rate fall to 0.6%.

The loan book remains well secured and of high quality, with an overall LTV of 50% with negligible losses emerging from the front book that has been developed in recent years.

Finally, Gilliat Financial Solutions reversed its financial progress made in the previous year by posting a loss of £0.4m (2012: profit £0.6m). This was due to overtrading during the year. Sales volumes actually increased by more than 20%, but in response to the positive signs from the IFA market, the business over purchased its stock of products and in the end had to discount its margins heavily. This strategy has been revised for 2014 and products are being purchased in line with demand from the IFAs rather than in advance. This should see the unit return to profitability in 2014.

Summarised Balance Sheet	2013 £000	2012 £000
Assets		
Loans and advances to customers	340,982	289,337
Liquid assets	239,168	231,209
Other assets (including Group balances)	39,523	48,069
Total assets	**619,673**	**568,615**
Liabilities		
Customer deposits	521,183	495,654
Other liabilities (including Group balances)	71,438	48,509
Total liabilities	592,621	544,163
Equity	27,052	24,452
Total equity and liabilities	**619,673**	**568,615**

Customer assets increased by 18% to close the year at £341.2m (2012: £289.3m), which was another year of robust growth, but still managed within our conservative risk appetite. Other assets reduced following the disposal of the Wilson Street property. Customer deposits again saw good inflows with balances increasing by 5%. But more importantly, the mix of deposits was rebalanced, with a number of higher yielding term balances maturing during the year being replaced by accounts with lower rates.

The loan to deposit ratio closed the year at 65% (2012: 59%) as the bank now has access to the FLS liquidity resources. This does allow the bank to operate a higher ratio, while maintaining a conservative policy with regard to liquidity.

The Private bank remains highly liquid and well capitalised with a total capital ratio of 12.8% (2012: 12.4%) and a core tier 1 ratio of 10.5% (2012: 9.9%).

Retail Banking - Secure Trust Bank

Summarised Income Statement	2013 £000	2012 £000
Net interest income	60,885	34,426
Net fee and commission income	18,097	12,582
Operating income	78,982	47,008
Gain from a bargain purchase	413	9,830
Other income	-	37
Operating expenses	(46,558)	(30,676)

Impairment losses - loans and advances	(15,644)	(8,946)
Profit after tax	**17,193**	**17,253**

The reported profit before tax is £17.2m (2012: £17.3m) which is largely unchanged on a statutory basis, however, the prior year results included a gain arising from the bargain purchase of Everyday Loans. The underlying profits have grown to £25.2m (2012: £16.8m) for the year, an increase of 51%.

The bank generated a 68% increase in operating income as the continued organic growth in the portfolios was augmented with the full year impact of the acquisitions made in 2012 and early 2013. An increase in high yielding customer assets and lower funding costs resulted in a 199 basis point widening of the blended customer net margin to 16.9% (2012: 15%).

Operating expenses increased by 51%, giving a positive operational leverage ratio of 21.7%. Included in expenses for the year were £1.2m (2012: £0.7m) related to the amortisation of the Everyday Loans intangible and £0.9m (2012: £nil) from the amortisation of the V12 intangible. Also, the cost of the STB share options was £2.2m (2012:£1.6m). Finally, STB also incurred acquisition costs of £0.9m (2012: £3.1m) during the year. The increase in the impairment losses was expected given the growth in the credit portfolios and the continued seasoning of customer accounts. However, the blended average loss rate was 4.3% (2012: 3.9%), still well below the levels anticipated at origination but higher as a result of the change in mix toward the higher yielding accounts.

The Current Account ended the year with 22,860 accounts (2012: 20,962) and Onebill with 24,297 (2012: 26,154).

Summarised Balance Sheet	2013 £000	2012 £000
Assets		
Asset finance		
Motor vehicles	114,570	89,620
Cycles	15,357	13,938
Musical instruments	8,818	6,700
V12	36,846	-
Personal computers	25,549	26,306
Pay4Later	26,899	16,776
DFS	917	469
Total asset finance	228,956	153,809
Personal lending	77,889	68,175
ELL	81,368	73,806
Commercial lending	1,784	-
Other lending	921	1,587
Acquired portfolios	110	254
Total loans and advances to customers	391,028	297,631
Liquid assets	71,958	130,442
Other assets (including Group balances)	56,611	46,526
Total assets	**519,597**	**474,599**
Liabilities		
Customer deposits	436,608	398,891
Other liabilities (including Group balances)	21,368	19,787
Total liabilities	457,976	418,678
Equity	61,621	55,921
Total equity and liabilities	**519,597**	**474,599**

During the year the asset finance portfolio increased by 49% with only the personal computer portfolio not growing. V12 added £36.8m during the year. Personal loans increased by 14% but growth was held back by delays in implementing the referral arrangement agreed with Sainsbury's Bank. Everyday Loans portfolio increased by 10% as caution has been exercised in the progression of this portfolio.

The bank remains entirely funded by retail deposits which increased by 9% to close the year at £433.4m (2012: £398.9m). The offering by the bank still remains attractive with market leading rates despite some downward corrections to rates during the year.

Group & Other Costs

Summarised Income Statement	2013 £000	2012 £000
Net interest income	(195)	122
Subordinated loan stock interest	(418)	(463)
Operating income	(613)	(341)
Other income	18	25
Gain on sale of subsidiary	-	839
Operating expenses	(8,363)	(7,235)
Impairment on financial investments	(249)	-
Profit after tax	**(9,207)**	**(6,712)**

Total Group costs increased to £9.2m (2012: £6.7m). This was a result of firstly, a lower level of operating income due to the conversion of the subordinated loan issued by STB into equity as part of the placing carried out in November 2012 and, secondly, the prior year containing a one off gain that arose on the sale of the Swiss banking subsidiary (£0.8m).

Group operating expenses increased by £1.1m due to higher salary and bonus awards along with the recognition of the 180 year anniversary (£0.4m) and additional provisions made in the Group's captive insurance cell (£0.3m).

Capital

The Group's capital management policy is focused on optimising shareholder value over the long term. There is a clear focus on delivering organic growth and ensuring capital resources are sufficient to support planned levels of growth. The Board regularly reviews the capital position.

In accordance with the EU's Capital Requirements Directive (CRD) and the required parameters set out in the PRA Handbook (BIPRU 2.2), the Individual Capital Adequacy Assessment Process (ICAAP) is embedded in the risk management framework of the Group and is subject to ongoing updates and revisions when necessary. However, at a minimum, the ICAAP is updated annually as part of the business planning process. The ICAAP is a process that brings together the management framework (i.e. the policies, procedures, strategies, and systems that the Group has implemented to identify, manage and mitigate its risks) and the financial disciplines of business planning and capital management.

The Group's regulated entities are also the principal trading subsidiaries as detailed in Note 42.

Not all material risks can be mitigated by capital, but where capital is appropriate the Board has adopted a "Pillar I plus" approach to determine the level of capital the Group needs to hold. This method takes the Pillar I capital formula calculations (standardised approach for credit, market and operational risk) as a starting point, and then considers whether each of the calculations deliver a sufficient capital sum adequate to cover management's anticipated risks. Where the Board considers that the Pillar I calculations does not reflect the risk, an additional capital add-on in Pillar II is applied.

The Group's regulatory capital is divided into two tiers:
• Tier 1 comprises mainly shareholders' funds and non-controlling interest, after deducting goodwill and other intangible assets.
• Lower Tier 2 comprises qualifying subordinated loan capital and revaluation reserves. Lower Tier 2 capital cannot exceed 50% of tier 1 capital.

The ICAAP includes a summary of the capital required to mitigate the identified risks in its regulated entities and the amount of capital that the Group has available. All regulated entities have complied with all of the externally imposed capital requirements to which they are subject.

Capital ratios	2013 £000	2012 £000
Core Tier 1 capital	87,270	68,508
Deductions	(11,405)	(7,309)
Tier 1 capital after deductions	75,865	61,199
Tier 2 capital	13,832	12,120
Total capital	**89,697**	**73,319**
Core Tier 1 capital ratio (Net Core Tier 1 capital/Basel 2 RWAs*)	**15.8%**	**15.5%**

Total Capital Ratio (Capital/Basel 2 RWAs*)	18.7%	18.5%

* - Risk Weighted Assets (RWAs)

In June 2013, the PRA published a final regulation to give effect to the Basel III framework, which amends the definition of Tier 1 capital. This comes into effect on 1 January 2014. The Group's current capital position is sufficient to meet the Tier 1 capital ratio based on the Tier 1 capital definition under the new regulation.

Risks and Uncertainties

The Group regards the monitoring and controlling of risks and uncertainties as a fundamental part of the management process. Consequently, senior management are involved in the development of risk management policies and in monitoring their application. A detailed description of risk management and their associated policies is set out in note 6 to the financial statements.

The principal risks inherent in the Group's business are credit, market, liquidity, operational and regulatory compliance.

Credit risk is the risk that a counterparty will be unable to pay amounts in full when due. This risk exists mainly in Arbuthnot Latham & Co., Limited and Secure Trust Bank PLC, which currently have loan books of £341.2m and £391.0m respectively. The lending portfolio in Arbuthnot Latham is extended to private banking clients, the majority of which is secured against cash, property or other assets. The portfolios within Secure Trust are extended to retail customers and are largely unsecured. Credit risk is managed through the Credit Committees of each bank with significant exposures also being approved by the Group Risk Committee.

Market risk arises in relation to movements in interest rates, currencies and equity markets. The Group's treasury function operates mainly to provide a service to clients and does not take significant unmatched positions in any market for its own account. Hence, the Group's exposure to adverse movements in interest rates and currencies is limited to interest earnings on its free cash and interest rate re-pricing mismatches.

Liquidity risk is the risk that the Group cannot meet its liabilities as they fall due. The Group takes a conservative approach to managing its liquidity profile. It has placed no reliance on the wholesale lending markets and is entirely funded by retail customer deposits. The loan to deposit ratios are maintained at prudent levels. Following introduction of the new liquidity regime, which came into force on 1 October 2010, the Group now maintains liquidity asset buffers which comprise high quality, unencumbered assets such as Government Securities, which can be called upon to meet the Group's liabilities.

Operational risk is the risk that the Group may be exposed to financial losses from conducting its business. The largest exposure to this risk exists in Arbuthnot Latham as mis-selling risk via its wealth management advisory service and its structured product distribution business. The Group is exposed to operational risks from its Information Technology and Operations platforms. There are additional internal controls in these processes that are designed to protect the Group from these risks. The Group's overall approach to managing internal control and financial reporting is described in the Corporate Governance section of the Annual Report.

As a financial services provider we face conduct risk, including selling products to customers which do not meet their needs; failing to deal with customers' complaints effectively; not meeting customers' expectations; and exhibiting behaviours which do not meet market or regulatory standards.

The Group maintains clear compliance guidelines and provides ongoing training to all staff. Periodic spot checks and internal audits are performed to ensure these guidelines are being maintained. The Group also has insurance policies in place to cover any claims that may arise.

Regulatory compliance risk is the risk that the Group will have insufficient capital resources to support the business or does not comply with regulatory requirements. The Group adopts a conservative approach to managing the capital of the Group. The principal regulated entities maintain capital ratios in excess of the minimum level set by the regulator. Capital requirements are forecast as part of the annual budgeting process and these are regularly monitored. Annually, the Group Board assesses the robustness of the capital requirements as part of the Individual Capital Adequacy Assessment Process (ICAAP) where stringent stress tests are performed to ensure that capital resources are adequate over a future three year horizon.

Dividend

The Board proposes a final dividend of 15 pence per share to be paid on 16 May 2014, giving a total dividend for the year of 44 pence (2012: 25 pence) per share, which include a special dividend of 18p paid in November 2013.

Going Concern

After making appropriate enquiries which assessed strategy, profitability, funding, risk management (see note 6) and capital resources (see note 7), the directors are satisfied that the Company and the Group have adequate resources to continue in operation for the foreseeable future. The financial statements are therefore prepared on the going concern basis.

James Cobb
Group Finance Director
19 March 2014

Group Directors' Report

The Directors submit their annual report and the audited consolidated financial statements for the year ended 31 December 2013.

Principal Activities and Review

The principal activities of the Group are banking and financial services. A strategic review in accordance with Section 414 C of the Companies Act 2006 forming part of this report is set out on pages 4 to 14.

Results and Dividends

The results for the year are shown on page 1. The profit after tax for the year of £11.5 million (2012: £11.1 million) is included in reserves.

The Company sold 580,000 ordinary 40p shares (3.7%) in its subsidiary Secure Trust Bank PLC on 13 December 2013 at a price of £25 per share. This resulted in a net gain of £14.4m which is also included in the Group's reserves.

The Directors recommend the payment of a final dividend of 15 pence on the ordinary shares which, together with the interim dividend of 11 pence paid on 4 October 2013 and a special dividend of 18p paid on 22 November 2013, represents total dividends for the year of 44 pence (2012: 25 pence). The final dividend, if approved by members at the Annual General Meeting, will be paid on 16 May 2014 to shareholders on the register at close of business on 18 April 2014.

Going Concern

After making appropriate enquiries which assessed strategy, profitability, funding, risk management (see note 6) and capital resources (see note 7), the directors are satisfied that the Company and the Group have adequate resources to continue in operation for the foreseeable future. The financial statements are therefore prepared on the going concern basis.

Share Capital

Shareholders will be asked to approve a Special Resolution renewing the authority of the Directors to make market purchases of shares not exceeding 10% of the existing issued share capital. The Directors will keep the position under review in order to maximise the Company's resources in the best interests of shareholders.

Remuneration

Shareholders will be asked to approve an Ordinary Resolution permitting bonus payments to be made to executive directors or senior managers not exceeding two times that director's annual basic salary if required by forthcoming regulation. It is the practice of the Company to pay fair and reasonable salaries and to reward exceptional performance under a bonus scheme. The Company seeks to keep down fixed overhead costs but does not welcome the principle of wage control.

Financial Risk Management

Details of how the Group manages risk are set out in in the Strategic Report and in note 6.

Substantial Shareholders

The Company was aware at 19 March 2014 of the following substantial holdings in the ordinary shares of the Company, other than those held by one director shown below:

Holder	Ordinary Shares	%
Prudential plc	625,161	4.2
Mr. R Paston	529,130	3.5

Directors

H Angest	*Chairman & CEO*
J R Cobb	*Finance Director*
J W Fleming	
Ms R J Lea	
P A Lynam	

Sir Christopher Meyer
A A Salmon *Chief Operating Officer*
R J J Wickham *Deputy Chairman*

All directors served throughout the year.

Mr. A.A. Salmon and Mr. P.A. Lynam retire under Article 78 of the Articles of Association and, being eligible, offer themselves for re-election. Both directors have service agreements terminable on twelve months' notice.

According to the information kept under Section 3 of the Disclosure and Transparency Rules 2006, the interests of directors and their families in the ordinary 1p shares of the Company at the dates shown were, and the percentage of the current issued share capital held is, as follows:

Beneficial Interests	1 January 2013	31 December 2013	18 March 2014	%
H Angest	8,186,901	8,200,901	8,200,901	53.7
J W Fleming	4,500	4,500	4,500	-
P A Lynam	10,000	10,000	10,000	0.1
A A Salmon	51,699	51,699	51,699	0.3
R J J Wickham	3,600	3,600	3,600	-

At the year end Mr. Lynam held 9,110 and Mr. Salmon 7,500 ordinary 40p shares in Secure Trust Bank PLC, a 67% subsidiary of the Company.

On 16 April 2013 Mr. Salmon exercised the option granted to him on 21 May 2008 to subscribe for 100,000 ordinary 1p shares in the Company at 337.5p and Mr. Cobb exercised the option granted to him on 5 November 2008 to subscribe for 50,000 ordinary 1p shares in the Company at 320p. The exercise price was 930p per share and the Board agreed to make a cash settlement rather than allot new shares.

On the same day Mr. Salmon and Mr. Cobb were granted new options to subscribe between April 2016 and April 2021 for 100,000 and 50,000 ordinary 1p shares respectively in the Company at 930p. The fair value of the options at grant date was £125k.

On 2 November 2011 Mr. Lynam and Mr. Salmon were each granted options to subscribe for 141,666 ordinary 40p shares in Secure Trust Bank PLC at 720p between 2 November 2014 and 1 November 2021, and a further 141,667 shares at 720p between 2 November 2016 and 1 November 2021. The fair value of the options at grant date was £1.6m.

Apart from the interests disclosed above, no director was interested at any time in the year in the share capital of Group companies.

No director, either during or at the end of the financial year, was materially interested in any contract with the Company or any of its subsidiaries, which was significant in relation to the Group's business. At 31 December 2013 three directors had loans from Arbuthnot Latham & Co., Limited amounting to £5,188,000, on normal commercial terms as disclosed in note 41 to the financial statements. At 31 December 2013 three directors had deposits with Secure Trust Bank PLC amounting to £265,000 and five directors had deposits with Arbuthnot Latham & Co., Limited amounting to £2,257,000, all on normal commercial terms as disclosed in note 41 to the financial statements.

The Company maintains insurance to provide liability cover for directors and officers of the Company.

Board Committees

The report of the Remuneration Committee on pages 21 and 22 will be the subject of an Ordinary Resolution at the Annual General Meeting.

Information on the Audit, Nomination, Risk and Donations Committees is included in the Corporate Governance section of the Annual Report on page 18 to 20.

Employees

The Company gives due consideration to the employment of disabled persons and is an equal opportunities employer. It also regularly provides employees with information on matters of concern to them, consults on decisions likely to affect their interests and encourages their involvement in the performance of the Company through share participation and in other ways.

Political Donations

The Company made a political donation of £27,000 to the Conservative Party during the year (2012: £50,000).

Auditors

Following a review of their corporate structure, our auditors KPMG Audit Plc, have instigated an orderly wind down of business, with future audit work being undertaken by KPMG LLP. The Board has decided to nominate KPMG LLP as auditors and a resolution for their appointment will be proposed at the forthcoming Annual General Meeting at a fee to be agreed in due course by the directors. There is no difference in liability terms between KPMG Audit Plc and KPMG LLP.

The Directors have disclosed to the auditors to the best of their knowledge and belief all relevant information necessary to assist the auditors in the preparation of their report.

By order of the Board

J R Kaye

Secretary
19 March 2014

Corporate Governance

AIM companies are not required to comply with The UK Corporate Governance Code ("The Code"). Nevertheless, the Board endorses the principles of openness, integrity and accountability which underlie good corporate governance and intends to take into account the provisions of The Code in so far as they are appropriate to the Group's size and circumstances. Moreover, the Group contains subsidiaries authorised to undertake regulated business under the Financial Services and Markets Act 2000 and regulated by the Prudential Regulatory Authority, including two which are authorised deposit taking businesses. Accordingly, the Group operates to the high standards of corporate accountability and regulatory compliance appropriate for such businesses.

Directors

The Group is led and controlled by an effective Board which comprises five executive directors and three non-executive directors.

The senior independent non-executive director is Robert Wickham, who in addition is Deputy Chairman. Although Mr. Wickham has served on the Board for twenty years from the date of his first election, he displays independence in both character and judgement and there are no other relationships or circumstances which could affect his judgement. Accordingly, the Board considers him to be independent.

The Board

The Board meets regularly throughout the year. Substantive agenda items have briefing papers, which are circulated in a timely manner before each meeting. The Board is satisfied that it is supplied with all the information that it requires and requests, in a form and of a quality to enable it to discharge its duties. In addition to ongoing matters concerning the strategy and management of the Company and of the Group, the Board has determined certain items which are reserved for decision by itself. These matters include the acquisition and disposal of other than minor businesses, the issue of capital by any Group company and any transaction by a subsidiary company that cannot be made within its own resources, or that is not in the normal course of its business.

The Company Secretary is responsible for ensuring that Board processes and procedures are appropriately followed and support effective decision making. All directors have access to the Company Secretary's advice and services and there is an agreed procedure for directors to obtain independent professional advice in the course of their duties, if necessary, at the Company's expense.

The Board has delegated certain of its responsibilities to Committees. All Committees have written terms of reference.

Audit Committee

Membership of the Audit Committee is limited to non-executive directors and comprises Ruth Lea (as Chairman), Sir Christopher Meyer and Robert Wickham.

The Audit Committee provides a forum for discussing with the Group's external auditors their report on the annual accounts, reviewing the scope, results and effectiveness of the internal audit work programme and considering any other matters which might have a financial impact on the Company, including the Group's arrangements by which staff may, in confidence, raise concerns about possible improprieties in matters of financial reporting or other matters. The Audit Committee's responsibilities include reviewing the Group's system of internal control and the process for evaluating and monitoring risk. The Committee also reviews the appointment, terms of engagement and objectivity of the external auditors, including the level of non-audit services provided, and ensures that there is an appropriate audit relationship.

Remuneration Committee

Information on the Remuneration Committee and details of the Directors' remuneration are set out in the separate Remuneration Report.

Nomination Committee

The Nomination Committee is chaired by Henry Angest and its other members are Robert Wickham and Ruth Lea. Before a Board appointment is made the skills, knowledge and experience required for a particular appointment are evaluated and a recommendation made to the Board.

Risk Committee

The Risk Committee is chaired by Henry Angest and its other members are James Cobb, James Fleming, John Reed (non-executive of Arbuthnot Latham), Paul Lynam (appointed 27 February 2014), Andrew Salmon and Robert Wickham. The role of the Risk Committee is to approve specific risk policies for Group subsidiaries and significant individual credit or other exposures.

Donations Committee

The Donations Committee is chaired by Henry Angest and its other members are Robert Wickham and Ruth Lea. The Committee considers any political donation or expenditure as defined within the Political Parties, Elections and Referendums Act 2000.

Shareholder Communications

The Company maintains a regular dialogue with its shareholders and makes full use of the Annual General Meeting and any other General Meetings to communicate with investors.

The Company aims to present a balanced and understandable assessment in all its reports to shareholders, its regulators and the wider public. Key announcements and other information can be found at: www.arbuthnotgroup.com.

Internal Control and Financial Reporting

The Board of directors has overall responsibility for the Group's system of internal control and for reviewing its effectiveness. Such a system is designed to manage rather than eliminate risk of failure to achieve business objectives and can only provide reasonable but not absolute assurance against the risk of material misstatement or loss.

The Directors and senior management of the Group have formally adopted a Group Risk and Controls Policy which sets out the Board's attitude to risk and internal control. Key risks identified by the Directors are formally reviewed and assessed at least once a year by the Board, in addition to which key business risks are identified, evaluated and managed by operating management on an ongoing basis by means of procedures such as physical controls, credit and other authorisation limits and segregation of duties. The Board also receives regular reports on any risk matters that need to be brought to its attention. Significant risks identified in connection with the development of new activities are subject to consideration by the Board. There are well-established budgeting procedures in place and reports are presented regularly to the Board detailing the results of each principal business unit, variances against budget and prior year, and other performance data.

The effectiveness of the internal control system is reviewed regularly by the Board and the Audit Committee, which also receives reports of reviews undertaken by the internal audit function which was outsourced to Ernst & Young. The Audit Committee also receives reports from the external auditors, KPMG Audit Plc, which include details of internal control matters that they have identified, as part of the Financial Statement audit. Certain aspects of the system of internal control are also subject to regulatory supervision, the results of which are monitored closely by the Board.

Statement of Directors' Responsibilities in Respect of the Strategic Report and the Directors' Report and the Financial Statements

The directors are responsible for preparing the Strategic Report and the Directors' Report and the financial statements in accordance with applicable law and regulations. Company law requires the Directors to prepare Group and Parent Company financial statements for each financial year. As required by the AIM Rules of the London Stock Exchange they are required to prepare the Group financial statements in accordance with IFRSs as adopted by the EU and applicable law and have elected to prepare the Parent Company financial statements on the same basis.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and Parent Company and of their profit or loss for that period. In preparing each of the Group and Parent Company financial statements, the Directors are required to:

• select suitable accounting policies and then apply them consistently;

• make judgments and estimates that are reasonable and prudent;

• state whether they have been prepared in accordance with IFRSs as adopted by the EU; and

• prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Group and the Parent Company will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the Parent Company and enable them to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Statement of Disclosure of Information to Auditors

The Directors confirm that:

• so far as each director is aware, there is no relevant audit information of which the Company's auditors are unaware; and

• the Directors have taken all the steps they ought to have taken as directors to make themselves aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

This confirmation is given and shall be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

Remuneration Report

Remuneration Committee

Membership of the Remuneration Committee is limited to non–executive directors together with Henry Angest as Chairman. The present members of the Committee are Henry Angest, Robert Wickham and Ruth Lea.

The Committee has responsibility for producing recommendations on the overall remuneration policy for directors and for setting the remuneration of individual directors, both for review by the Board. Members of the Committee do not vote on their own remuneration.

Remuneration Policy

The Remuneration Committee determines the remuneration of individual directors having regard to the size and nature of the business; the importance of attracting, retaining and motivating management of the appropriate calibre without paying more than is necessary for this purpose; remuneration data for comparable positions; the need to align the interests of executives with those of shareholders; and an appropriate balance between current remuneration and longer term performance–related rewards. The remuneration package can comprise a combination of basic annual salary and benefits (including pension), a discretionary annual bonus award related to the Committee's assessment of the contribution made by the executive during the year and longer term incentives, including executive share options. Pension benefits take the form of annual contributions paid by the Company to individual money purchase schemes. The Remuneration Committee reviews salary levels each year based on the performance of the Group during the preceding financial period. This review does not necessarily lead to increases in salary levels. During 2011 the Group implemented all the provisions required under the FCA Remuneration Code. Accordingly the Group and its subsidiaries are all considered to be Tier 3 institutions.

Remuneration Resolution

Shareholders will be asked to approve an Ordinary Resolution permitting bonus payments to be made to executive directors or senior managers not exceeding two times that director's annual basic salary if required by forthcoming regulation. It is the practice of the Company to pay fair and reasonable salaries and to reward exceptional performance under a bonus scheme. The company seeks to keep down fixed overhead costs but does not welcome the principle of wage control.

Directors' Service Contracts

Henry Angest, James Fleming, Paul Lynam and Andrew Salmon each have service contracts terminable at any time on 12 months' notice in writing by either party. James Cobb has a service contract terminable at any time on 6 months' notice in writing by either party.

Share Option and Long Term Incentive Schemes

This part of the remuneration report is audited information.

In May 2005, the Company extended its Unapproved Executive Share Option Scheme for a further period of 10 years.

The Company has an ESOP ("the Arbuthnot ESOP Trust") under which trustees may purchase shares in the Company to satisfy the exercise of share options by employees including executive directors.

On 16 April 2013 Mr. Salmon exercised the option granted to him on 21 May 2008 to subscribe for 100,000 ordinary 1p shares in the Company at 337.5p and Mr. Cobb exercised the option granted to him on 5 November 2008 to subscribe for 50,000 ordinary 1p shares in the Company at 320p. The exercise price was 930p per share and the Board agreed to make a cash settlement rather than allot new shares.

On the same day Mr. Salmon and Mr. Cobb were granted new options to subscribe between April 2016 and April 2021 for 100,000 and 50,000 ordinary 1p shares respectively in the Company at 930p. The fair value of the options at grant date was £125k.

At the date of this remuneration report, the only outstanding options to directors under the Unapproved Executive Share Option Scheme are those in relation to 100,000 shares for Andrew Salmon and 50,000 shares for James Cobb. 150,500 shares are held in the Arbuthnot ESOP Trust.

Under the Unapproved Executive Share Option Scheme of the Company's subsidiary, Secure Trust Bank PLC, established in November 2011, Paul Lynam and Andrew Salmon were each granted options over 283,333 shares in that company. The fair value of the options at grant date was £1.6m.

Directors' Emoluments

This part of the remuneration report is audited information.

	2013 £000	2012 £000
Fees (including benefits in kind)	215	215
Salary payments (including benefits in kind)	3,328	3,027
Pension contributions	140	137
Long term incentive	897	-
	4,580	**3,379**

	Salary £000	Bonus £000	Benefits £000	Pension £000	Fees £000	Long term incentive £000	Total 2013 £000	Total 2012 £000
H Angest	475	-	40	-	-	-	515	519
JR Cobb	235	200	16	35	-	305	791	436
JW Fleming (from 01/03/12)	230	225	15	35	-	-	505	458
PA Lynam	475	500	21	35	-	-	1,031	870
DM Proctor (to 01/03/12)	-	-	-	-	-	-	-	49
AA Salmon	475	400	21	35	-	592	1,523	832
Ms RJ Lea	-	-	-	-	120	-	120	120
Sir Christopher Meyer	-	-	-	-	45	-	45	45
RJJW Wickham	-	-	-	-	50	-	50	50
	1,890	**1,325**	**113**	**140**	**215**	**897**	**4,580**	**3,379**

Details of any shares or options held by directors are presented on page 16.

The emoluments of the Chairman were £515,000 (2012: £519,000). The emoluments of the highest paid director were £1,523,000 (2012: £870,000) including pension contributions of £35,000 (2012: £35,000).

Mr. R J J Wickham is a director of Calando Finance Limited which received an annual fee of £50,000 (2012: £50,000) in respect of his services to the Group.

These amounts are included in the table above.

Retirement benefits are accruing under money purchase schemes for five directors who served during 2013 (2012: six directors).

Henry Angest
Chairman of the Remuneration Committee
19 March 2014

Independent Auditor's Report

We have audited the financial statements of Arbuthnot Banking Group PLC for the year ended 31 December 2013 set out on pages 25 to 85. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU and, as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As explained more fully in the Directors' Responsibilities Statement set out on page 19, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

Opinion on financial statements

In our opinion:

• the financial statements give a true and fair view of the state of the Group's and of the Parent Company's affairs as at 31 December 2013 and of the Group's profit for the year then ended;

• the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the EU;

• the Parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the EU and as applied in accordance with the provisions of the Companies Act 2006; and

• the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matters prescribed by the Companies Act 2006 and under the terms of our engagement

In our opinion the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

• adequate accounting records have not been kept by the Parent Company, or returns adequate for our audit have not been received from branches not visited by us; or

• the Parent Company financial statements are not in agreement with the accounting records and returns; or

• certain disclosures of directors' remuneration specified by law are not made; or

• we have not received all the information and explanations we require for our audit.

Richard Gabbertas (Senior Statutory Auditor)
for and on behalf of KPMG Audit Plc, Statutory Auditor
Chartered Accountants

15 Canada Square
London
E14 5GL
19 March 2014

Company statement of financial position

	Note	At 31 December 2013 £000	2012 £000
ASSETS			
Due from subsidiary undertakings - bank balances		16,551	-
Financial investments	26	165	413
Deferred tax asset		441	447
Intangible assets	29	12	20
Property, plant and equipment	30	130	134
Other assets	25	5,415	5,662
Investment in subsidiary undertakings	42	30,995	30,847
Total assets		**53,709**	**37,523**
EQUITY AND LIABILITIES			
Equity			
Share capital	36	153	153
Other reserves	37	(1,030)	(1,030)
Retained earnings	37	31,325	20,768
Total equity		**30,448**	**19,891**
LIABILITIES			
Bank overdraft		2,000	100
Other liabilities	33	9,029	5,552
Debt securities in issue	34	12,232	11,980
Total liabilities		**23,261**	**17,632**
Total equity and liabilities		**53,709**	**37,523**

The Company has elected to take the exemption under section 408 of the Companies Act 2006 not to present the Parent Company profit and loss account. The profit for the Parent Company for the year is presented in the Statement of Changes in Equity.

Consolidated statement of changes in equity

	Attributable to equity holders of the Group										
	Share capital	Share premium account	Foreign currency translation reserve	Revaluation reserve	Capital redemption reserve	Available -for-sale reserve	Cash flow hedging reserve	Treasury shares	Retained earnings	Non-controlling interests	Total
	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000
Balance at 1 January 2013	**153**	**-**	**-**	**140**	**20**	**81**	**(363)**	**(1,131)**	**53,372**	**16,376**	**68,648**
Total comprehensive income for the period											
Profit for 2013	-	-	-	-	-	-	-	-	7,930	3,585	11,515
Other comprehensive income, net of tax											
Revaluation reserve											
- Adjustment	-	-	-	51	-	-	-	-	(35)	(16)	-
Cash flow hedging reserve											
- Effective portion of changes in fair value	-	-	-	-	-	-	(15)	-	-	-	(15)
Available-for-sale reserve	-	-	-	-	-	(250)	-	-	-	-	(250)
Total other comprehensive income	**-**	**-**	**-**	**51**	**-**	**(250)**	**(15)**	**-**	**(35)**	**(16)**	**(265)**
Total comprehensive income for the period	**-**	**-**	**-**	**51**	**-**	**(250)**	**(15)**	**-**	**7,895**	**3,569**	**11,250**
Transactions with owners, recorded directly in equity											
Contributions by and distributions to owners											
Equity settled share based payment transactions	-	-	-	-	-	-	-	-	901	770	1,671
Sale of shares Secure Trust Bank	-	-	-	-	-	-	-	-	12,135	2,270	14,405
Final dividend relating to 2012	-	-	-	-	-	-	-	-	(2,084)	(1,970)	(4,054)
Interim dividend relating to 2013	-	-	-	-	-	-	-	-	(1,638)	(688)	(2,326)
Special dividend relating to 2013	-	-	-	-	-	-	-	-	(2,680)	-	(2,680)
Total contributions by and distributions to owners	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**6,634**	**382**	**7,016**
Balance at 31 December 2013	**153**	**-**	**-**	**191**	**20**	**(169)**	**(378)**	**(1,131)**	**67,901**	**20,327**	**86,914**

	Attributable to equity holders of the Group										
	Share capital	Share premium account	Foreign currency translation reserve	Revaluation reserve	Capital redemption reserve	Available -for-sale reserve	Cash flow hedging reserve	Treasury shares	Retained earnings	Non-controlling interests	Total
	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000	£000
Balance at 1 January 2012	**153**	**21,085**	**(570)**	**140**	**20**	**-**	**(329)**	**(1,097)**	**21,571**	**5,998**	**46,971**
Total comprehensive income for the period											
Profit for 2012	-	-	-	-	-	-	-	-	8,041	3,077	11,118
Other comprehensive income, net of tax											
Foreign currency translation reserve	-	-	570	-	-	-	-	-	-	-	570
Revaluation reserve											
Cash flow hedging reserve											

- Effective portion of changes in fair value	-	-	-	-	-	-	(34)	-	-	-	(34)
Available-for-sale reserve	-	-	-	-	-	81	-	-	-	-	81
Total other comprehensive income	**-**	**-**	**570**	**-**	**-**	**81**	**(34)**	**-**	**-**	**-**	**617**
Total comprehensive income for the period	**-**	**-**	**570**	**-**	**-**	**81**	**(34)**	**-**	**8,041**	**3,077**	**11,735**
Transactions with owners, recorded directly in equity											
Contributions by and distributions to owners											
Cancellation of share premium	-	(21,085)	-	-	-	-	-	-	21,085	-	-
Purchase of own shares	-	-	-	-	-	-	-	(34)	-	-	(34)
Equity settled share based payment transactions	-	-	-	-	-	-	-	-	-	(70)	(70)
Share placing Secure Trust Bank	-	-	-	-	-	-	-	-	6,881	7,371	14,252
Final dividend relating to 2011	-	-	-	-	-	-	-	-	(2,082)	-	(2,082)
Interim dividend relating to 2012	-	-	-	-	-	-	-	-	(2,124)	-	(2,124)
Total contributions by and distributions to owners	**-**	**(21,085)**	**-**	**-**	**-**	**-**	**-**	**(34)**	**23,760**	**7,301**	**9,942**
Balance at 31 December 2012	**153**	**-**	**-**	**140**	**20**	**81**	**(363)**	**(1,131)**	**53,372**	**16,376**	**68,648**

Company statement of changes in equity

	Attributable to equity holders of the Company						
	Share capital	Share premium account	Capital redemption reserve	Available -for-sale reserve	Treasury shares	Retained earnings	Total
	£000	£000	£000	£000	£000	£000	£000
Balance at 1 January 2012	**153**	**21,085**	**20**	**-**	**(1,097)**	**8,517**	**28,678**
Total comprehensive income for the period							
Loss for 2012	-	-	-	-	-	(5,260)	(5,260)
Other comprehensive income, net of income tax							
Available-for-sale reserve	-	-	-	81	-	-	81
Total other comprehensive income	**-**	**-**	**-**	**81**	**-**	**-**	**81**
Total comprehensive income for the period	**-**	**-**	**-**	**81**	**-**	**(5,260)**	**(5,179)**
Transactions with owners, recorded directly in equity							
Contributions by and distributions to owners							
Cancellation of share premium	-	(21,085)	-	-	-	21,085	-
Purchase of own shares	-	-	-	-	(34)	-	(34)
Final dividend relating to 2011	-	-	-	-	-	(1,936)	(1,936)
Interim dividend relating to 2012	-	-	-	-	-	(1,638)	(1,638)
Total contributions by and distributions to owners	**-**	**(21,085)**	**-**	**-**	**(34)**	**17,511**	**(3,608)**
Balance at 1 January 2013	**153**	**-**	**20**	**81**	**(1,131)**	**20,768**	**19,891**
Total comprehensive income for the period							
Profit for 2013	-	-	-	-	-	17,828	17,828
Other comprehensive income, net of income tax							

Total comprehensive income for the period	**-**	**-**	**-**	**-**	**-**	**17,828**	**17,828**
Transactions with owners, recorded directly in equity							
Contributions by and distributions to owners							
Share based payments settled in cash	-	-	-	-	-	(897)	(897)
Equity settled share based payment transactions	-	-	-	-	-	28	28
Final dividend relating to 2012	-	-	-	-	-	(2,084)	(2,084)
Interim dividend relating to 2013	-	-	-	-	-	(1,638)	(1,638)
Special dividend relating to 2013	-	-	-	-	-	(2,680)	(2,680)
Total contributions by and distributions to owners	**-**	**-**	**-**	**-**	**-**	**(7,271)**	**(7,271)**
Balance at 31 December 2013	**153**	**-**	**20**	**81**	**(1,131)**	**31,325**	**30,448**

Consolidated statement of cash flows

	Note	Year ended 31 December 2013 £000	Year ended 31 December 2012 £000
Cash flows from operating activities			
Interest received		91,075	61,957
Interest paid		(20,085)	(13,405)
Fees and commissions received		26,325	20,769
Net trading and other income		7,718	11,065
Cash payments to employees and suppliers		(81,157)	(64,182)
Taxation paid		(2,543)	(4,083)
Cash flows from operating profits before changes in operating assets and liabilities		21,333	12,121
Changes in operating assets and liabilities:			
- net decrease in derivative financial instruments		49	765
- net increase in loans and advances to customers		(122,682)	(132,312)
- net (increase)/decrease in other assets		(3,572)	3,616
- net increase in deposits from banks		1,630	365
- net increase in amounts due to customers		61,945	200,745
- net increase in other liabilities		6,990	5,096
Net cash (outflow)/inflow from operating activities		**(34,307)**	**90,396**
Cash flows from investing activities			
Borrowings repaid on acquisition of subsidiary undertakings	10, 44	(36,922)	(71,618)
Cash acquired on purchase of subsidiary undertakings	10, 44	1,512	991
Purchase of subsidiary undertakings	10, 44	(4,026)	-
Acquisition of financial investments		-	(93)
Disposal of financial investments		63	-
Purchase of computer software	29	(1,162)	(662)
Disposal of computer software	29	1,900	-
Purchase of property, plant and equipment	30	(746)	(17,661)
Investment in associate	28	(943)	-
Proceeds from sale of property, plant and equipment		23,259	12
Purchases of debt securities		(9,844)	(51,523)
Proceeds from redemption of debt securities		3,904	78,076
Net cash from investing activities		**(23,005)**	**(62,478)**
Cash flows from financing activities			
Purchase of treasury shares		-	(34)
Increase in borrowings		2,000	-
Dividends paid		(9,060)	(4,206)
Proceeds from share placing by Secure Trust Bank		-	14,252
Proceeds from sale of Secure Trust Bank shares		14,405	-

	Note		
Net cash used in financing activities		**7,345**	**10,012**
Net (decrease)/increase in cash and cash equivalents		(49,967)	37,930
Cash and cash equivalents at 1 January		348,074	310,144
Cash and cash equivalents at 31 December	40	**298,107**	**348,074**

Company statement of cash flows

	Note	Year ended 31 December 2013 £000	Year ended 31 December 2012 £000
Cash flows from operating activities			
Dividends received from subsidiaries		11,418	1,947
Interest received		99	278
Interest paid		(714)	(631)
Net trading and other income		1,364	1,075
Cash payments to employees and suppliers		(8,089)	(8,298)
Taxation received		(160)	(7)
Cash flows from operating profits/(losses) before changes in operating assets and liabilities		3,918	(5,636)
Changes in operating assets and liabilities:			
- net decrease in group company balances		3,128	1,061
- net decrease/(increase) in other assets		254	(357)
- net increase/(decrease) in other liabilities		348	(3,762)
Net cash inflow/(outflow) from operating activities		**7,648**	**(8,694)**
Cash flows from investing activities			
Increase in loans to subsidiary companies		-	(2,000)
Repayment of loans to subsidiary companies		-	6,500
Increase investment in subsidiary		(1,000)	(6,000)
Disposal of share in subsidiaries		14,405	386
Purchase of property, plant and equipment	30	-	(13)
Net cash from investing activities		**13,405**	**(1,127)**
Cash flows from financing activities			
Purchase of treasury shares		-	(34)
Dividends paid		(6,402)	(3,574)
Increase in borrowings		2,000	100
Net cash used in financing activities		**(4,402)**	**(3,508)**
Net increase/(decrease) in cash and cash equivalents		16,651	(13,329)
Cash and cash equivalents at 1 January		(100)	13,329
Cash and cash equivalents at 31 December		**16,551**	**-**

Notes to the Consolidated Financial Statements

1. Reporting entity

Arbuthnot Banking Group PLC is a company domiciled in United Kingdom. The registered address of the Arbuthnot Banking Group PLC is One Arleston Way, Solihull B90 4LH. The consolidated financial statements of the Arbuthnot Banking Group PLC as at and for the year ended 31 December 2013 comprise the Arbuthnot Banking Group PLC and its subsidiaries (together referred to as the "Group" and individually as "subsidiaries"). The Company is primarily involved in banking and financial services.

2. Basis of presentation

(a) Statement of compliance

The Group's consolidated financial statements and the Company's financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs as adopted and endorsed by the EU) and the Companies Act 2006 applicable to companies reporting under IFRS.

The consolidated financial statements were authorised for issue by the Board of Directors on 19 March 2014.

(b) Basis of measurement
The consolidated and company financial statements have been prepared under the historical cost convention, as modified by the revaluation of land and buildings, available-for-sale financial assets, financial assets and financial liabilities at fair value through profit or loss, and derivatives assets and liabilities.

(c) Functional and presentational currency
Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in Pound Sterling, which is the Company's functional and the Group's presentational currency.

(d) Use of estimates and judgements
The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

(e) Accounting developments
• IAS 1 (Revised), 'Presentation of Financial Statements – Presentation of items of other comprehensive income' (effective 1 July 2012). The revised standard require the split of other comprehensive income between items which may subsequently be reclassified to profit or loss and items that will not be reclassified to profit or loss. The disclosure of other comprehensive income on the face of the Statement of Comprehensive Income in these financial statements has been changed to reflect this split.

• IFRS 7 (Revised), 'Disclosures - Offsetting Financial Assets and Financial Liabilities' (effective 1 January 2013). The revised standard amend the required disclosures to include information that will enable users of an entity's financial statements to evaluate the effect or potential effect of netting arrangements, including rights of set-off associated with the entity's recognised financial assets and recognised financial liabilities, on the entity's financial position. This change did not have any material impact on the financial statements.

• IFRS 13, 'Fair Value Measurement' (effective 1 January 2013). This standard replaces the existing guidance on fair value measurement in different IFRSs with a single definition of fair value, a framework for measuring fair values and disclosures about fair value measurements.

(f) Going concern
The Group's business activities and financial position, its objectives and policies in managing the financial risks to which it is exposed, and its capital, the factors likely to affect its future development and performance, are discussed in the Financial Review. The Directors have assessed, in the light of current and anticipated economic conditions, the Group's ability to continue as a going concern. The Directors confirm they are satisfied that the Company and the Group have adequate resources to continue in business for the foreseeable future. For this reason, they continue to adopt the 'going concern' basis for preparing accounts.

3. Significant accounting policies

The accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

3.1. Consolidation
(a) Subsidiaries

Subsidiaries are all entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies, generally accompanying a shareholding of more than one-half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

The acquisition method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired, liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest. The excess of the cost of acquisition over the fair value of the Group's shares of the identifiable net assets acquired is recorded as

goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the Statement of Comprehensive Income.

The Parent's investments in subsidiaries are recorded at cost less, where appropriate, provisions for impairment in value. Changes in the Parent's ownership interest in a subsidiary that do not result in a loss of control are treated as transactions between equity holders and are reported in equity.

Inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

(b) Special purpose entities
Special purpose entities (SPEs) are entities that are created to accomplish a narrow and well-defined objective such as the securitisation of particular assets, or the execution of a specific borrowing or lending transaction. SPEs are consolidated when the substance of the relationship between the Group and the entity and the evaluation of the Group's exposure to the risks and rewards of the SPE indicates control. The following circumstances may indicate control by the Group and would therefore require consolidation of the SPE:

• in substance, the activities of the SPE are being conducted on behalf of the entity according to its specific business needs so that the entity obtains benefits from the SPE's operation;

• in substance, the entity has the decision-making powers to obtain the majority of the benefits of the activities of the SPE or, by setting up an 'autopilot' mechanism, the entity has delegated these decision-making powers;

• in substance, the entity has rights to obtain the majority of the benefits of the SPE and therefore may be exposed to risks incident to the activities of the SPE; or

• in substance, the entity retains the majority of the residual or ownership risks related to the SPE or its assets in order to obtain benefits from its activities.

The assessment of whether the Group has control over an SPE is carried out at inception and the initial assessment is only reconsidered at a later date if there were any changes to the structure or terms of the SPE, or there were additional transactions between the Group and the SPE.

(c) Associates
Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Significant influence is presumed to exist when the Group holds between 20 and 50 percent of the voting power of another entity. Associates are accounted for using the equity method and are initially recognised at cost. The Group's investment includes goodwill identified on acquisition, net of any accumulated impairment losses. The consolidated financial statements include the Group's share of the total comprehensive income and equity movements of equity accounted investees, from the date that significant influence commences until the date that significant influence ceases. When the Group's share of losses exceeds its interest in an equity accounted investee, the Group's carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the investee.

(d) Transactions and non-controlling interests
Changes in ownership interest in a subsidiary that do not result in the loss of control are accounted for as equity transactions and no gain or loss is recognised. Adjustments to non-controlling interests are based on a proportionate amount of the net assets of the subsidiary.

3.2. Segment reporting
Operating segments are reported in a manner consistent with the internal reporting provided to the Group Board. The Group Board, which is responsible for allocating resources and assessing performance of the operating segments, has been identified as the chief operating decision maker. All transactions between segments are conducted on an arm's length basis. Income and expenses directly associated with each segment are included in determining segment performance. There are three main operating segments:

• Retail Banking
• Private Banking
• Group Centre

3.3. Foreign currency translation
(a) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation where items are remeasured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the Statement of Comprehensive Income.

(b) Group companies

The results and financial position of all the Group entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentational currency are translated into the presentation currency as follows:

• assets and liabilities for each Statement of Financial Position presented are translated at the closing rate at the date of that Statement of Financial Position;

• income and expenses for each Statement of Comprehensive Income are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions); and

• all resulting exchange differences are recognised as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign operations, and of borrowings and other currency instruments designated as hedges of such investments, are taken to shareholders' equity. When a foreign operation is partially disposed of or sold, exchange differences that were recorded in equity are recognised in the Statement of Comprehensive Income as part of the gain or loss on sale.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity are treated as assets and liabilities of the foreign entity and translated at the closing rate.

3.4. Interest income and expense

Interest income and expense are recognised in the Statement of Comprehensive Income for all instruments measured at amortised cost using the effective interest method.

The effective interest method calculates the amortised cost of a financial asset or a financial liability and allocates the interest income or interest expense over the relevant period. The effective interest rate is the rate that discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group takes into account all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts. The carrying amount of the financial asset or financial liability is adjusted if the Group revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income continues to be recognised using the original effective interest rate applied to the new carrying amount.

3.5. Fee and commission income

Fees and commissions which are not considered integral to the effective interest rate are generally recognised on an accrual basis when the service has been provided. Loan commitment fees are deferred and recognised as an adjustment to the effective interest rate on the loan.

Commission and fees arising from negotiating, or participating in the negotiation of, a transaction for a third party — such as the issue or the acquisition of shares or other securities or the purchase or sale of businesses — are recognised on completion of the underlying transaction. Asset and other management, advisory and service fees are recognised based on the applicable service contracts, usually on a time apportioned basis. The same principle is applied for financial planning and insurance services that are continuously provided over an extended period of time. Commissions arising from the sale of structured products are recognised at the point of sale as there are no further services provided or due.

3.6. Financial assets and financial liabilities

The Group classifies financial assets and financial liabilities in the following categories: financial assets and financial liabilities at fair value through profit or loss; loans and receivables; held-to-maturity investments; available-for-sale financial assets and other financial liabilities. Management determines the classification of its investments at acquisition. A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

(a) Financial assets and financial liabilities at fair value through profit or loss
This category comprises listed securities and derivative financial instruments. Derivative financial instruments utilised by the Group include embedded derivatives and derivatives used for hedging purposes. Financial assets and liabilities at fair value through profit or loss are initially recognised on the date from which the Group becomes a party to the contractual provisions of the instrument. Subsequent measurement of financial assets and financial liabilities held in this category are carried at fair value through profit or loss.

(b) Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable. Loans are recognised when cash is advanced to the borrowers. Loans and receivables are carried at amortised cost using the effective interest method.

(c) Held-to-maturity
Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity. Held-to-maturity investments are carried at amortised cost using the effective interest method.

(d) Available-for-sale
Available-for-sale ('AFS') investments are those not classified as another category of financial assets. These include investments in special purpose vehicles and equity investments in unquoted vehicles. They may be sold in response to liquidity requirements, interest rate, exchange rate or equity price movements. AFS investments are initially recognised at cost, which is considered as the fair value of the investment including any acquisition costs. AFS securities are subsequently carried at fair value in the statement of financial position. Fair value changes on the AFS securities are recognised directly in equity (AFS reserve) until the investment is sold or impaired. Once sold or impaired, the cumulative gains or losses previously recognised in the AFS reserve are recycled to the profit or loss.

(e) Other financial liabilities
Other financial liabilities are non-derivative financial liabilities with fixed or determinable payments. Other financial liabilities are recognised when cash is received from the depositors. Other financial liabilities are carried at amortised cost using the effective interest method. The fair value of other liabilities repayable on demand is assumed to be the amount payable on demand at the Statement of Financial Position date.

Derecognition
Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risks and rewards of ownership. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Group is recognised as a separate asset or liability in the Statement of Financial Position. In transactions which the Group neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset and it retains control over the asset, the Group continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset. There have not been any instances where assets have only been partially derecognised.

The Group derecognises a financial liability when its contractual obligations are discharged, cancelled, expire, are modified or exchanged.

Amortised cost measurement
The amortised cost of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured at initial recognition, minus principal payments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, less any reduction for impairment.

Fair value measurement
Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

When available, the Group measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, the Group establishes fair value using a valuation technique. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same for which market observable prices exist, net present value and discounted cash flow analysis.

In the instance that fair values of assets and liabilities cannot be reliably measured, they are carried at cost.

3.7. Derivative financial instruments and hedge accounting

All derivatives are recognised at their fair value. Fair values are obtained from quoted market prices in active markets, including recent arm's length transactions or using valuation techniques such as discounted cash flow models. Derivatives are shown in the Statement of Financial Position as assets when their fair value is positive and as liabilities when their fair value is negative.

(a) Fair value hedges

Fair value hedges are used to hedge against the change in fair value of a recognised asset or liability or a firm commitment that could affect profit or loss. Changes in the fair value of the derivative are recognised immediately in profit or loss together with changes in the fair value of the hedged item that are attributable to the hedged risk (in the same line item in the profit or loss as the hedged item).

If the hedging derivative expires or is sold, terminated or exercised, or the hedging relationship no longer meets the criteria for hedge accounting, the carrying amount of the hedged item is amortised over the residual period to maturity, as part of the newly calculated effective interest rate. However, if the hedged item has been derecognised, it is immediately released to the profit or loss.

(b) Cash flow hedges

These cash flow hedges are used to hedge against fluctuations in future cash flows from interest rate movements on variable rate customer deposits. On initial purchase the derivative is valued at fair value and then the effective portion of the change in the fair value of the hedging instrument is recognised in equity (cash flow hedging reserve) until the gain or loss on the hedged item is realised, when it is amortised; the ineffective portion of the hedging instrument is recognised in the immediately in the profit or loss.

If a hedging derivative expires or is sold, terminated, or exchanged, or the hedge no longer meets the criteria for cash flow hedge accounting, or the hedge designation is revoked, then hedge accounting is discontinued prospectively. In a discontinued hedge of a forecast transaction the cumulative amount recognised in other comprehensive income from the period when the hedge was effective is reclassified from equity to profit or loss as a reclassification adjustment when the forecast transaction occurs and affects profit or loss. If the forecast transaction is no longer expected to occur, then the balance in other comprehensive income is reclassified immediately to profit or loss as a reclassification adjustment.

Hedge effectiveness testing

On initial designation of the hedge, the Group formally documents the relationship between the hedging instruments and the hedged items, including the risk management objective and strategy in undertaking the hedge, together with the method that will be used to assess the effectiveness of the hedging relationship. The Group makes an assessment, both at the inception of the hedge relationship as well as on an ongoing basis, as to whether the hedging instruments are expected to be highly effective in offsetting the changes in the fair value or cash flows of the respective hedged items during the period for which the hedge is designated, and whether the actual results of each hedge are within a range of 80-125%. The Group makes an assessment for a cash flow hedge of a forecast transaction, as to whether the forecast transaction is highly probable to occur and presents an exposure to variations in cash flows that could ultimately affect profit or loss.

(c) Embedded derivatives

Embedded derivatives arise from contracts (‘hybrid contracts’) containing both a derivative (the ‘embedded derivative’) and a non-derivative (the ‘host contract’). Where the economic characteristics and risks of the embedded derivatives are not closely related to those of the host contract, and the host contract is not at fair value through profit of loss, the embedded derivative is bifurcated and reported at fair value and gains or losses are recognised in the Statement of Comprehensive Income.

3.8. Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the Statement of Financial Position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

3.9. Impairment of financial assets

(a) Assets carried at amortised cost

On an ongoing basis the Group assesses whether there is objective evidence that a financial asset or group of financial assets is impaired. Objective evidence is the occurrence of a loss event, after the initial recognition of the asset, that impact on the estimated future cash flows of the financial asset or group of financial assets, and can be reliably estimated.

The criteria that the Group uses to determine that there is objective evidence of an impairment loss include, but are not limited to, the following:

- Delinquency in contractual payments of principal or interest;
- Cash flow difficulties experienced by the borrower;
- Initiation of bankruptcy proceedings;
- Deterioration in the value of collateral;

• Deterioration of the borrower's competitive position;

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the Statement of Comprehensive Income. If a loan or held-to maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. When a loan is uncollectible, it is written off against the related provision for loan impairment. Subsequent recoveries of amounts previously written off decrease the amount of the provision for loan impairment in the Statement of Comprehensive Income.

(b) Assets classified as available-for-sale

The Group assesses at each Statement of Financial Position date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered as an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the Statement of Comprehensive Income. Impairment losses recognised in the Statement of Comprehensive Income on equity instruments are not reversed through the Statement of Comprehensive Income.

(c) Renegotiated loans

Loans that are either subject to collective impairment assessment or individually significant and whose terms have been renegotiated are no longer considered to be past due but are treated as new loans.

(d) Forbearance

Forbearance is available to support customers who are in financial difficulty and help them re-establish their contractual payment plan. The main option offered by the Group is an arrangement to clear outstanding arrears. If the forbearance request is granted the account is monitored in accordance with the Group's policy and procedures. All debts however retain the customer's normal contractual payment due dates. Arrears tracking and the allowance for impairment is based on the original contractual due dates for both the secured and unsecured lending channels.

3.10 Inventory

Land acquired through repossession of collateral which is subsequently held in the ordinary course of business with a view to develop and sell is accounted for as inventory.

Inventory is measured at the lower of cost or net realisable value. The cost of inventories comprise of all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

3.11. Intangible assets

(a) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary or associate at the date of acquisition. Goodwill on acquisitions of subsidiaries or associates is included in 'intangible assets'. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

The Group reviews the goodwill for impairment at least annually or when events or changes in economic circumstances indicate that impairment may have taken place and carry goodwill at cost less accumulated impairment losses. Assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit" or "CGU"). For impairment testing purposes goodwill cannot be allocated to a CGU that is greater than a reported operating segment. CGUs to which goodwill has been allocated are aggregated so that the level at which impairment is tested reflects the lowest level at which goodwill is monitored for internal reporting purposes. Goodwill acquired in a business combination is allocated to groups of CGUs that are expected to benefit from the synergies of the combination. The test for impairment involves comparing the carrying value of goodwill with the present value of pre-tax cash flows, discounted at a rate of interest that reflects the inherent risks of the CGU to which the goodwill relates, or the CGU's fair value if this is higher.

(b) Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised on the basis of the expected useful lives (three to five years).

Costs associated with developing or maintaining computer software programs are recognised as an expense as incurred.

(c) Other intangibles
Other intangibles include trademarks, customer relationships, broker relationships, technology and banking licences acquired. These costs are amortised on the basis of the expected useful lives (three to ten years).

3.12. Property, plant and equipment

Land and buildings comprise mainly branches and offices and are stated at the latest valuation with subsequent additions at cost less depreciation. Plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Land is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, applying the following annual rates, which are subject to regular review:

Freehold buildings	50 years
Office equipment	6 to 20 years
Computer equipment	3 to 5 years
Motor vehicles	4 years

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the Statement of Comprehensive Income. Depreciation on revalued freehold buildings is calculated using the straight-line method over the remaining useful life. Revaluation of assets and any subsequent disposals are addressed through the revaluation reserve and any changes are transferred to retained earnings.

3.13. Leases

(a) As a lessor
Assets leased to customers under agreements which transfer substantially all the risks and rewards of ownership, with or without ultimate legal title, are classified as finance leases. When assets are held subject to finance leases, the present value of the lease payments is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income. Lease income is recognised over the term of the lease using the net investment method, which reflects a constant periodic rate of return.

Assets leased to customers under agreements which do not transfer substantially all the risks and rewards of ownership are classified as operating leases. When assets are held subject to operating leases, the underlying assets are held at cost less accumulated depreciation, The assets are depreciated down to their estimated residual values on a straight line basis over the lease term. Lease rental income is recognised on a straight line basis over the lease term.

(b) As a lessee
Rentals made under operating leases are recognised in the Statement of Comprehensive Income on a straight line basis over the term of the lease.

Leases in which the Group assumes substantially all the risks and rewards of ownership of the leased asset are classified as finance leases. Leased assets by way of finance leases are stated at an amount equal to the lower of their fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation. Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

3.14. Cash and cash equivalents

For the purposes of the Statement of Cash Flows, cash and cash equivalents comprises cash on hand and demand deposits, and cash equivalents are deemed highly liquid investments that are convertible into cash with an insignificant risk of changes in value with a maturity of three months or less at the date of acquisition.

3.15. Employee benefits

(a) Post-retirement obligations
The Group contributes to a defined contribution scheme and to individual defined contribution schemes for the benefit of certain employees. The schemes are funded through payments to insurance companies or trustee-administered funds at the contribution rates agreed with individual employees.

The Group has no further payment obligations once the contributions have been paid. The contributions are recognised as an employee benefit expense when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payments is available.

There are no post-retirement benefits other than pensions.

(b) Share-based compensation
The fair value of equity settled share-based payment awards are calculated at grant date and recognised over the period in which the employees become unconditionally entitled to the awards (the vesting period). The amount is recognised as personnel expenses in the profit and loss, with a corresponding increase in equity. The Group adopts a Black-Scholes valuation model in calculating the fair value of the share options as adjusted for an attrition rate of members of the scheme and a probability of pay-out reflecting the risk of not meeting the terms of the scheme over the vesting period. The number of share options that are expected to vest are reviewed at least annually.

The fair value of cash settled share-based payments is recognised as personnel expenses in the profit or loss with a corresponding increase in liabilities over the vesting period. The liability is remeasured at each reporting date and at settlement date based on the fair value of the options granted, with a corresponding adjustment to personnel expenses.

When share-based payments are changed from cash settled to equity settled and there is no change in the fair value of the replacement award, it is seen as a modification to the terms and conditions on which the equity instruments were granted and is not seen as the settlement and replacement of the instruments. Accordingly, the liability in the Statement of Financial Position is reclassified to equity and the prospective charge to the profit or loss from the modification reflects the spreading of the initial grant date fair value of the award over the remaining vesting period in line with the policy on equity settled awards.

3.16. Taxation
Current income tax which is payable on taxable profits is recognised as an expense in the period in which the profits arise. Income tax recoverable on tax allowable losses is recognised as an asset only to the extent that it is regarded as recoverable by offset against current or future taxable profits.

Deferred tax is provided in full on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred tax is not accounted for if it arises from the initial recognition of goodwill, the initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss, and differences relating to investments in subsidiaries to the extent that they probably will not reverse in the foreseeable future. Deferred tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the Statement of Financial Position date and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to taxes levied by the same tax authority on the same taxable entity, or on different tax entities, when they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

Deferred tax assets are recognised where it is probable that future taxable profits will be available against which the temporary differences can be utilised.

3.17. Issued debt and equity securities
Issued financial instruments or their components are classified as liabilities where the contractual arrangement results in the Group having a present obligation to either deliver cash or another financial asset to the holder, to exchange financial instruments on terms that are potentially unfavourable. Issued financial instruments, or their components, are classified as equity where they meet the definition of equity and confer on the holder a residual interest in the assets of the Company. The components of issued financial instruments that contain both liability and equity elements are accounted for separately with the equity component being assigned the residual amount after deducting from the instrument as a whole the amount separately determined as the fair value of the liability component.

Financial liabilities, other than trading liabilities at fair value, are carried at amortised cost using the effective interest method as set out in policy 1.6. Equity instruments, including share capital, are initially recognised at net proceeds, after deducting transaction costs and any related income tax. Dividend and other payments to equity holders are deducted from equity, net of any related tax.

3.18. Share capital
(a) Share issue costs
Incremental costs directly attributable to the issue of new shares or options or the acquisition of a business by Arbuthnot Banking Group or its subsidiaries, are shown in equity as a deduction, net of tax, from the proceeds.

(b) Dividends on ordinary shares
Dividends on ordinary shares are recognised in equity in the period in which they are approved.

(c) Share buybacks

Where any Group company purchases the Company's equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the Company's equity holders until the shares are cancelled or reissued.

3.19. Financial guarantee contracts

Financial guarantees represent undertakings that the Group will meet a customer's obligation to third parties if the customer fails to do so. Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. The Group is theoretically exposed to loss in an amount equal to the total guarantees or unused commitments, however, the likely amount of loss is expected to be significantly less; most commitments to extend credit are contingent upon customers maintaining specific credit standards. Liabilities under financial guarantee contracts are initially recorded at their fair value, and the initial fair value is amortised over the life of the financial guarantee. Subsequently, the financial guarantee liabilities are measured at the higher of the initial fair value, less cumulative amortisation, and the best estimate of the expenditure to settle obligations.

3.20. Fiduciary activities

The Group commonly acts as trustees and in other fiduciary capacities that result in the holding or placing of assets on behalf of individuals, trusts, retirement benefit plans and other institutions. These assets and income arising thereon are excluded from these financial statements, as they are not assets of the Group.

3.21. New standards and interpretations not yet adopted

The following standards, interpretations and amendments to existing standards have been published and are mandatory for the Group's accounting periods beginning on or after 1 January 2014 or later periods, but the Group has not early adopted them:

• IFRS 10, 'Consolidated Financial Statements' and IAS 27 (Revised), 'Separate Financial Statements' (effective 1 January 2013). IFRS 10 supersedes IAS 27 and SIC-12, and provides a single model to be applied in the control analysis for all investees. There are some minor clarifications in IAS27, and the requirements of IAS 28 and IAS 31 have been incorporated into IAS 27. [1]

• IFRS 11, 'Joint Arrangements' (effective 1 January 2013). This standard replaces the existing accounting for subsidiaries and joint ventures (now joint arrangements) and removes the choice of equity or proportionate accounting for jointly controlled entities, as was the case under IAS 31. [1]

• IFRS 12, 'Disclosure of Interests in Other Entities' (effective 1 January 2013). This standard replaces the existing accounting for subsidiaries and joint ventures (now joint arrangements) and contains the disclosure requirements for entities that have interests in subsidiaries, joint arrangements, associates and/or unconsolidated structured entities. [1]
• IAS 32 (Revised), 'Offsetting Financial Assets and Financial Liabilities' (effective 1 January 2014). This standard was amended to clarify the offsetting criteria, specifically when an entity currently has a legal right of set off; and when gross settlement is equivalent to net settlement.

• IFRIC 21, 'Levies' (effective 1 January 2014). The interpretation defines a levy as an outflow from an entity imposed by a government in accordance with legislation. That levy is recognised as a liability when, and only when, the triggering event specified in the legislation occurs. [2]

The above standards are unlikely to have a material impact on the Group.

• IFRS 9, 'Financial instruments' (effective from 1 January 2015). This standard deals with the classification and measurement of financial assets and will replace IAS 39. The requirements of this standard represent a significant change from the existing requirements in IAS 39. The standard contains two primary measurement categories for financial assets: amortised cost and fair value. The standard eliminates the existing IAS 39 categories of 'held to maturity', 'available for sale' and ' loans and receivables'. Further development phases for IFRS 9 are scheduled to cover key areas such as impairment and hedge accounting. The potential effect of this standard together with the further development phases are currently being evaluated but it is expected to have a material impact on the Group's financial statements, due to the nature of the Group's operations. [2]

[1] - These standards have been endorsed by the EU for periods from 1 January 2014.
[2] - These standards have not yet been endorsed by the EU.

4. Critical accounting estimates and judgements in applying accounting policies

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

4.1 Credit losses

The Group reviews its loan portfolios and held-to-maturity investments to assess impairment at least on a half-yearly basis. The basis for evaluating impairment losses is described in accounting policy 3.10. Where financial assets are individually evaluated for impairment, management uses their best estimates in calculating the net present value of future cash flows. Management has to make judgements on the financial position of the counterparty and the net realisable value of collateral, in determining the expected future cash flows.

In determining whether an impairment loss should be recorded in the Statement of Comprehensive Income, the Group makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans or held-to-maturity investments with similar credit characteristics, before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the Group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Where financial assets are individually evaluated for impairment, management uses their best estimates in calculating the net present value of future cash flows. Management has to make judgements on the financial position of the counterparty and the net realisable value of collateral (where held), in determining the expected future cash flows.

In assessing collective impairment the Group uses historical trends of the probability of default, the timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be significantly different to historic trends.

To the extent that the default rates differ from that estimated by 10%, the allowance for impairment on loans and advances would change by an estimated £2.6m (2012: £1.6m).

4.2 Goodwill impairment

The accounting policy for goodwill is described in note 3.11 (a). The Company reviews the goodwill for impairment at least annually or when events or changes in economic circumstances indicate that impairment may have taken place. Significant management judgements are made in estimations, to evaluate whether an impairment of goodwill is necessary. Impairment testing is done at CGU level and the following two items, with judgements surrounding them, have a significant impact on the estimations used in determining the necessity of an impairment charge:

• Future cash flows - Cash flow forecasts reflect management's view of future business forecasts at the time of the assessment. A detailed three year budget is done every year and management also uses judgement in applying a growth rate. The accuracy of future cash flows is subject to a high degree of uncertainty in volatile market conditions. During such conditions, management would do impairment testing more frequently than annually to ensure that the assumptions applied are still valid in the current market conditions.
• Discount rate - Management also apply judgement in determining the discount rate used to discount future expected cash flows. The discount rate is derived from the cost of capital for each CGU.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. There are currently three CGU's (2012: two) with goodwill attached; the core Arbuthnot Latham CGU, the Music Finance CGU and the V12 Group CGU (subsidiary of Secure Trust Bank acquired in the year).

Management considers the value in use for the core Arbuthnot Latham CGU to be the discounted cash flows over 5 years with a terminal value (2012: 5 years with a terminal value). The 5 year discounted cash flows with a terminal value is considered to be appropriate as the goodwill relates to an ongoing well established business and not underlying assets with finite lives. The terminal value is calculated by applying a discounted perpetual growth model to the profit expected in 2016 as per the approved 3 year plan. A growth rate of 9% (2012: 9%) was used for income and 7% (2012: 5%) for expenditure from 2014 to 2016 (these rates were the best estimate of future forecasted performance), while a 3% (2012: 3%) percent growth rate for income and expenditure (a more conservative approach was taken for latter years as these were not budgeted for in detail as per the three year plan approved by the Board of Directors) was used for cash flows after the approved three year plan.

Management considers the value in use for the Music Finance CGU and V12 Group CGU to be the discounted cash flows over 5 years (2012: 5 years). Income and expenditure were kept flat (2012: 0%) over the 5 year period.

Cash flows were discounted at a pre-tax rate of 12% (2012: 12%) to their net present value. The discount rate of 12% is considered to be appropriate after evaluating current market assessments of the time value of money and the risks specific to the assets or CGUs. Currently the value in use and fair value less costs to sell far exceeds the carrying value and as such no sensitivity analysis was done.

At the time of the impairment testing, if the future expected cash flows decline and/or the cost of capital has increased, then the recoverable amount will reduce.

4.3 Taxation

The Group is subject to direct and indirect taxation in a number of jurisdictions. There may be some transactions and calculations for which the ultimate tax determination has an element of uncertainty during the ordinary course of business. The Group recognises liabilities based on estimates of the quantum of taxes that may be due. Where the final tax determination is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax expense in the year in which the determination is made.

4.4 Acquisition accounting

The Group recognises identifiable assets and liabilities at their acquisition date fair values. The exercise of attributing a fair value to the balance sheet of the acquired entity requires the use of a number of assumptions and estimates, which are documented at the time of the acquisition. These fair value adjustments are determined from the estimated future cash flows generated by the assets.

Loans and advances to customers

The methodology of attributing a fair value to the loans and advances to customers involves discounting the estimated future cashflows after impairment losses, using a risk adjusted discount factor. A fair value adjustment is then applied to the carrying value in the acquiree's balance sheet.

Intangible assets

Identifying the separately identifiable intangible assets of an acquired company is subjective and based upon discussions with management and a review of relevant documentation. During the current and prior years the acquisition of Everyday Loans and the V12 Finance Group indicated that there were four separately identifiable intangible assets which met the criteria for separation from goodwill, these being Trademarks/Tradenames, Customer Relationships, Broker Relationships and Technology.

Trademarks and Tradenames are valued by estimating the fair value of the estimated costs savings resulting from the ownership of trade names as opposed to licensing them. Customer Relationships are valued through the application of a discounted cashflow methodology to net anticipated renewal revenues. The valuation of Broker Relationships is derived from a costs avoided methodology, by reviewing costs incurred on non-broker platforms versus costs which are incurred in broker commission. Technology is valued by the market derived royalty rate applied to the related cash flows to arrive at estimated savings resulting from the use of the acquired credit decisioning technology.

4.5 Average life of lending

IAS 39 requires interest earned from lending to be measured under the effective interest rate method. The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset.

Management must therefore use judgement to estimate the expected life of each instrument and hence the expected cash flows relating to it. The accuracy of the effective interest rate would therefore be affected by unexpected market movements resulting in altered customer behaviour, inaccuracies in the models used compared to actual outcomes and incorrect assumptions.

4.6 Share option scheme valuation

The valuation of the Secure Trust Bank equity-settled share option scheme was determined at the original grant date of 2 November 2011 using Black-Scholes valuation models. In the opinion of the directors the terms of the scheme are such that there remain a number of key uncertainties to be considered when calculating the probability of pay out, which are set out below. The directors also considered the probability of option holder attrition prior to the vesting dates, details of which are also set out below.

Much of the bank's lending is in the near and sub-prime categories, with performance of the book heavily influenced by employment trends. With the UK economy remaining fragile, the impact of a further downturn would be increasing unemployment, potentially causing impairments to rise and new business levels to fall, thereby affecting the bank's ability to sustain the levels of dividend growth required under the terms of the scheme. Depending on the product type, market and customer demographics, the bank's current product range includes expected lifetime losses of between 1% and 20%.

Uncertainties in the regulatory environment continue, with pressure on the government to further constrain the activities of banks following the well reported catalogue of recent issues in the industry. Any tightening of capital requirements will impact on the ability of the Company to exploit future market opportunities and furthermore may inhibit its ability to maintain the required growth in distributions.

Taking these into account, the probability of pay out has been judged as 95% for the first tranche of share options (SOS1) which vest on 2 November 2014 and 80% for the second tranche of share options (SOS2) which vest on 2 November 2016.

One participant in the share option scheme left the Company during 2012 and was consequently withdrawn from the scheme. The directors consider that there is further uncertainty surrounding whether the remaining participants will all still be in situ and eligible at the vesting date. The directors have assumed an attrition rate of 8% for the 2014 options and an attrition rate of 15% for the 2016 options over the scheme period.

4.7 Impairment of equity securities

A significant or prolonged decline in the fair value of an equity security is objective evidence of impairment. The Group regards a decline of more than 20 percent in fair value as "significant" and a decline in the quoted market price that persists for nine months or longer as "prolonged".

4.8 Valuation of financial instruments

The Group measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions. If a market for a financial instrument is not active, the Group establishes fair value using a valuation technique. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same for which market observable prices exist, net present value and discounted cash flow analysis. The objective of valuation techniques is to determine the fair value of the financial instrument at the reporting date as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. In the instance that fair values of assets and liabilities cannot be reliably measured, they are carried at cost.

The Group measures fair value using the following fair value hierarchy that reflects the significance of the inputs used in making measurements:

- Level 1: Quoted prices in active markets for identical assets or liabilities
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The consideration of factors such as the magnitude and frequency of trading activity, the availability of prices and the size of bid/offer spreads, assist in the judgement as to whether a market is active. If in the opinion of management, a significant proportion of the instrument's carrying amount is driven by unobservable inputs, the instrument in its entirety is classified as valued using significant unobservable inputs. 'Unobservable' in this context means that there is little or no current market data available from which to determine the level at which an arm's length transaction would be likely to occur. It generally does not mean that there is no market data available at all upon which to base a determination of fair value (consensus pricing data may, for example, be used).

The tables below analyses financial instruments measured at fair value by the level in the fair value hierarchy into which the measurement is categorised:

At 31 December 2013	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Derivative financial instruments	-	508	-	508
Financial investments	179	-	1,796	1,975
Asset	**179**	**508**	**1,796**	**2,483**
Derivative financial instruments	-	371	-	371
Liability	**-**	**371**	**-**	**371**

At 31 December 2012	Level 1 £000	Level 2 £000	Level 3 £000	Total £000
Derivative financial instruments	-	648	-	648
Financial investments	489	-	2,768	3,257
Asset	**489**	**648**	**2,768**	**3,905**
Derivative financial instruments	-	462	-	462

Liability	-	462	-	462

5. Maturity analysis of assets and liabilities

The table below shows the maturity analysis of assets and liabilities of the Group as at 31 December 2013:

At 31 December 2013	Due within one year £000	Due after more than one year £000	Total £000
ASSETS			
Cash	193,046	-	193,046
Loans and advances to banks	105,061	-	105,061
Debt securities held-to-maturity	19,466	-	19,466
Derivative financial instruments	488	20	508
Loans and advances to customers	419,694	312,315	732,009
Other assets	13,699	3,568	17,267
Financial investments	-	1,975	1,975
Deferred tax asset	-	3,954	3,954
Investment in associate	-	943	943
Intangible assets	-	13,103	13,103
Property, plant and equipment	-	5,522	5,522
Total assets	**751,454**	**341,400**	**1,092,854**
LIABILITIES			
Deposits from banks	2,003	-	2,003
Derivative financial instruments	371	-	371
Deposits from customers	781,468	176,323	957,791
Current tax liability	1,427	-	1,427
Other liabilities	26,702	4,315	31,017
Deferred tax liability	-	1,099	1,099
Debt securities in issue	-	12,232	12,232
Total liabilities	**811,971**	**193,969**	**1,005,940**

The table below shows the maturity analysis of assets and liabilities of the Group as at 31 December 2012:

At 31 December 2012	Due within one year £000	Due after more than one year £000	Total £000
ASSETS			
Cash	203,683	-	203,683
Loans and advances to banks	144,391	-	144,391
Debt securities held-to-maturity	13,526	-	13,526
Derivative financial instruments	623	25	648
Loans and advances to customers	347,460	239,508	586,968
Other assets	9,080	2,586	11,666
Financial investments	-	3,257	3,257
Deferred tax asset	-	5,057	5,057
Intangible assets	-	8,326	8,326
Property, plant and equipment	100	22,387	22,487
Total assets	**718,863**	**281,146**	**1,000,009**
LIABILITIES			
Deposits from banks	373	-	373
Derivative financial instruments	462	-	462
Deposits from customers	749,672	144,873	894,545
Current tax liability	346	-	346
Other liabilities	18,416	4,605	23,021

Deferred tax liability	-	634	634
Debt securities in issue	-	11,980	11,980
Total liabilities	**769,269**	**162,092**	**931,361**

The table below shows the maturity analysis of assets and liabilities of the Company as at 31 December 2013:

At 31 December 2013	Due within one year £000	Due after more than one year £000	Total £000
ASSETS			
Due from subsidiary undertakings - bank balances	16,551	-	16,551
Financial investments	-	165	165
Deferred tax asset	-	441	441
Intangible assets	-	12	12
Property, plant and equipment	-	130	130
Other assets	565	4,850	5,415
Shares in subsidiary undertakings	-	30,995	30,995
Total assets	**17,116**	**36,593**	**53,709**
LIABILITIES			
Deposit from bank	2,000	-	2,000
Other liabilities	9,029	-	9,029
Debt securities in issue	-	12,232	12,232
Total liabilities	**11,029**	**12,232**	**23,261**

The table below shows the maturity analysis of assets and liabilities of the Company as at 31 December 2012:

At 31 December 2012	Due within one year £000	Due after more than one year £000	Total £000
ASSETS			
Financial investments	-	413	413
Deferred tax asset	421	26	447
Intangible assets	-	20	20
Property, plant and equipment	-	134	134
Other assets	812	4,850	5,662
Shares in subsidiary undertakings	-	30,847	30,847
Total assets	**1,233**	**36,290**	**37,523**
LIABILITIES			
Due to subsidiary undertakings - bank balances	100	-	100
Other liabilities	5,552	-	5,552
Debt securities in issue	-	11,980	11,980
Total liabilities	**5,652**	**11,980**	**17,632**

6. Financial risk management

Strategy

By their nature, the Group's activities are principally related to the use of financial instruments. The Directors and senior management of the Group have formally adopted a Group Risk and Controls Policy which sets out the Board's attitude to risk and internal controls. Key risks identified by the Directors are formally reviewed and assessed at least once a year by the Board, in addition to which key business risks are identified, evaluated and managed by operating management on an ongoing basis by means of procedures such as physical controls, credit and other authorisation limits and segregation of duties. The Board also receives regular reports on any risk matters that need to be brought to its attention. Significant risks identified in connection with the development of new activities are subject to consideration by the Board. There are budgeting procedures in place and reports are presented regularly to the Board detailing the results of each principal business unit, variances against budget and prior year, and other performance data.

The principal non-operational risks inherent in the Group's business are credit, market and liquidity risks.

(a) Credit risk

The Company and Group take on exposure to credit risk, which is the risk that a counterparty will be unable to pay amounts in full when due. Impairment provisions are provided for losses that have been incurred at the balance sheet date. Significant changes in the economy, or in the health of a particular industry segment that represents a concentration in the Company and Group's portfolio, could result in losses that are different from those provided for at the balance sheet date. Credit risk is managed through the Credit Committees of the banking subsidiaries, with significant exposures also being approved by the Group Risk Committee.

The Company and Group structure the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower or groups of borrowers. Such risks are monitored on a revolving basis and subject to an annual or more frequent review. The limits are approved periodically by the Board of Directors and actual exposures against limits are monitored daily.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees.

The Group employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of collateral to secure advances, which is common practice. The principal collateral types for loans and advances include, but are not limited to:

- Charges over residential and commercial properties;
- Charges over business assets such as premises, inventory and accounts receivable;
- Charges over financial instruments such as debt securities and equities;
- Personal guarantees; and
- Charges over other chattels

Upon initial recognition of loans and advances, the fair value of collateral is based on valuation techniques commonly used for the corresponding assets. In order to minimise any potential credit loss the Group will seek additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances. Repossessed collateral, not readily convertible into cash, is made available for sale in an orderly fashion, with the proceeds used to reduce or repay the outstanding indebtedness, or held as inventory where the Group intends to develop and sell in the future. Where excess funds are available after the debt has been repaid, they are available either for other secured lenders with lower priority or are returned to the customer.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Group is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards.

The Group's maximum exposure to credit risk before collateral held or other credit enhancements is as follows:

	2013 £000	2012 £000
Credit risk exposures relating to on-balance sheet assets are as follows:		
Cash	193,046	203,683
Loans and advances to banks	105,061	144,391
Debt securities held-to-maturity	19,466	13,526
Derivative financial instruments	508	648
Loans and advances to customers - Arbuthnot Latham	340,981	289,337
Loan and advances to customers - Secure Trust Bank	391,028	297,631
Financial investments	1,975	3,257
Other assets	6,135	3,393
Credit risk exposures relating to off-balance sheet assets are as follows:		
Guarantees	805	879
Loan commitments and other credit related liabilities	37,094	21,491
At 31 December	**1,096,099**	**978,236**

The Company's maximum exposure to credit risk before collateral held or other credit enhancements is as follows:

	2013 £000	2012 £000
Credit risk exposures relating to on-balance sheet assets are as follows:		

Due from subsidiary undertakings - bank balances	16,551	-
Financial investments	165	413
Other assets	5,310	5,309
Credit risk exposures relating to off-balance sheet assets are as follows:		
Guarantees	2,500	2,500
At 31 December	**24,526**	**8,222**

The above table represents the maximum credit risk exposure (net of impairment) to the Group and Company at 31 December 2013 and 2012 without taking account of any collateral held or other credit enhancements attached. For on-balance-sheet assets, the exposures are based on the net carrying amounts as reported in the Statement of Financial Position.

The table below represents an analysis of the loan to values of the property book for the Group:

	31 December 2013		31 December 2012	
	Loan Balance	Collateral	Loan Balance	Collateral
Loan to value	£000	£000	£000	£000
Less than 60%	176,713	464,460	144,250	344,543
60% - 80%	94,295	136,786	82,462	121,832
80% - 100%	24,188	26,907	21,407	25,463
Greater than 100%	17,089	13,816	25,000	19,433
Total	**312,285**	**641,969**	**273,119**	**511,271**

Forbearance

Arbuthnot Latham and Secure Trust Bank generally do not reschedule contractual arrangements where customers default on their repayments. Under its Treating Customers Fairly policies however, the company may offer the customer the option to reduce or defer payments for a short period. If the request is granted, the account continues to be monitored in accordance with the Group's impairment provisioning policy. Such debts retain the customer's normal contractual payment due dates and will be treated the same as any other defaulting cases for impairment purposes. Arrears tracking will continue on the account with any impairment charge being based on the original contractual due dates for all products.

In June 2012, the Group acquired Everyday Loans whose policy on forbearance is that a customers' account may be modified to assist customers who are in or, have recently overcome, financial difficulties and have demonstrated both the ability and willingness to meet the current or modified loan contractual payments. These may be modified by way of a reschedule or deferment of repayments. Rescheduling of debts retains the customers contractual due dates, whilst the deferment of repayments extends the payment schedule up to a maximum of four payments in a 12 month period. As at 31 December 2013 the gross balance of rescheduled loans included in the consolidated statement of financial position was £13.9 million, with an allowance for impairment on these loans of £1.1 million. The gross balance of deferred loans was £2.8 million with an allowance for impairment on these of £0.4 million (2012: the gross balance of rescheduled loans was £12.3 million, with an allowance for impairment on these loans of £1.2 million and the gross balance of deferred loans was £2.9 million with an allowance for impairment on these of £0.4 million.

Concentration risk

The Group is well diversified in the UK, being exposed to retail banking and private banking. Management assesses the potential concentration risk from a number of areas including:
- geographical concentration
- product concentration; and
- high value residential properties

Due to the well diversified nature of the Group and the significant collateral held against the loan book, the Directors do not consider there to be a potential material exposure arising from concentration risk.

(b) Operational risk

The Group's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Group's reputation with overall cost effectiveness and to avoid control procedures that restrict initiatives and creativity. Operational risk arises from all of the Group's operations.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to the senior management within each subsidiary.

Compliance with Group standards is supported by a programme of periodic reviews undertaken by Internal Audit. The results of the Internal Audit reviews are discussed with senior management, with summaries submitted to the Arbuthnot Banking Group Audit Committee.

(c) Market risk

Price risk

The Company and Group is exposed to equity securities price risk because of investments held by the Group and classified on the Consolidated Statement of Financial Position either as available-for-sale or at fair value through the profit and loss. The Group is not exposed to commodity price risk. To manage its price risk arising from investments in equity securities, the Group diversifies its portfolio. Diversification of the portfolio is done in accordance with the limits set by the Group.

Based upon the financial investment exposure (in Note 26), a stress test scenario of a 10% (2012: 10%) decline in market prices, with all other things being equal, would result in a £394,000 (2012: £17,000) decrease in the Group's income and a decrease of £140,000 (2012: £255,000) in the Group's equity. The Group consider a 10% stress test scenario appropriate after taking the current values and historic data into account.

Based upon the financial investment exposure given in Note 26, a stress test scenario of a 10% (2012: 10%) decline in market prices, with all other things being equal, would result in a £15,000 (2012: £17,000) decrease in the Company's income and a decrease of £13,000 (2012: £13,000) in the Company's equity.

Currency risk

The Company and Group takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Board sets limits on the level of exposure for both overnight and intra-day positions, which are monitored daily. The table below summarises the Group's exposure to foreign currency exchange rate risk at 31 December 2013. Included in the table below are the Group's assets and liabilities at carrying amounts, categorised by currency.

	GBP (£)	USD ($)	Euro (€)	Other	Total
At 31 December 2013	£000	£000	£000	£000	£000
ASSETS					
Cash	192,972	53	20	1	193,046
Loans and advances to banks	85,365	16,703	1,160	1,833	105,061
Debt securities held-to-maturity	16,423	3,043	-	-	19,466
Derivative financial instruments	508	-	-	-	508
Loans and advances to customers	682,925	3,748	45,336	-	732,009
Other assets	9,678	-	-	-	9,678
Financial investments	179	-	1,796	-	1,975
	988,050	**23,547**	**48,312**	**1,834**	**1,061,743**
LIABILITIES					
Deposits from banks	2,003	-	-	-	2,003
Derivative financial instruments	371	-	-	-	371
Deposits from customers	916,465	20,292	19,388	1,646	957,791
Other liabilities	10,152	-	-	-	10,152
Debt securities in issue	-	-	12,232	-	12,232
	928,991	**20,292**	**31,620**	**1,646**	**982,549**
Net on-balance sheet position	**59,059**	**3,255**	**16,692**	**188**	**79,194**
Credit commitments	**37,899**	**-**	**-**	**-**	**37,899**

The table below summarises the Group's exposure to foreign currency exchange risk at 31 December 2012:

	GBP (£)	USD ($)	Euro (€)	Other	Total
At 31 December 2012	£000	£000	£000	£000	£000
ASSETS					
Cash	203,638	16	27	2	203,683

Loans and advances to banks	132,202	9,713	738	1,738	144,391
Debt securities held-to-maturity	13,526	-	-	-	13,526
Derivative financial instruments	648	-	-	-	648
Loans and advances to customers	541,745	4,236	40,985	2	586,968
Other assets	11,604	62	-	-	11,666
Financial investments	515	-	2,742	-	3,257
	903,878	**14,027**	**44,492**	**1,742**	**964,139**
LIABILITIES					
Deposits from banks	373	-	-	-	373
Derivative financial instruments	462	-	-	-	462
Deposits from customers	861,329	14,469	17,019	1,728	894,545
Other liabilities	23,021	-	-	-	23,021
Debt securities in issue	-	-	11,980	-	11,980
	885,185	**14,469**	**28,999**	**1,728**	**930,381**
Net on-balance sheet position	**18,693**	**(442)**	**15,493**	**14**	**33,758**
Credit commitments	**22,370**	**-**	**-**	**-**	**22,370**

A 10% strengthening of the pound against the US dollar would lead to a £5,000 increase (2012: £44,000 decrease) in Group profits and equity, while a 10% weakening of the pound against the US dollar would lead to the same decrease in Group profits and equity. Similarly a 10% strengthening of the pound against the Euro would lead to a £20,000 increase (2012: £86,000 decrease) in Group profits and equity, while a 10% weakening of the pound against the Euro would lead to the same increase in Group profits and equity. The above results are after taking into account the effect of derivative financial instruments (see note 22), which covers most of the net exposure in each currency.

The table below summarises the Company's exposure to foreign currency exchange rate risk at 31 December 2013:

At 31 December 2013	GBP (£) £000	Euro (€) £000	Total £000
ASSETS			
Due from subsidiary undertakings - bank balances	3,827	12,724	16,551
Financial investments	165	-	165
Other assets	5,310	-	5,310
Investment in subsidiary undertakings	30,995	-	30,995
	40,297	**12,724**	**53,021**
LIABILITIES			
Deposits from banks	2,000	-	2,000
Other liabilities	7,768	-	7,768
Debt securities in issue	-	12,232	12,232
	9,768	**12,232**	**22,000**
Net on-balance sheet position	**30,529**	**492**	**31,021**

The table below summarises the Company's exposure to foreign currency exchange rate risk at 31 December 2012:

At 31 December 2012	GBP (£) £000	Euro (€) £000	Total £000
ASSETS			
Financial investments	413	-	413
Other assets	5,309	-	5,309
Investment in subsidiary undertakings	30,847	-	30,847
	36,569	**-**	**36,569**
LIABILITIES			
Due to subsidiary undertakings - bank balances	12,600	(12,500)	100
Other liabilities	4,639	-	4,639
Debt securities in issue	-	11,980	11,980

	17,239	**(520)**	**16,719**
Net on-balance sheet position	**19,330**	**520**	**19,850**

A 10% strengthening of the pound against the Euro would lead to £24,000 (2012: £26,000) decrease in the Company profits and equity, conversely a 10% weakening of the pound against the Euro would lead to the same increase in the Company profits and equity.

Interest rate risk

Interest rate risk is the potential adverse impact on the Company and Group's future cash flows from changes in interest rates; and arises from the differing interest rate risk characteristics of the Company and Group's assets and liabilities. In particular, fixed rate savings and borrowing products expose the Group to the risk that a change in interest rates could cause either a reduction in interest income or an increase in interest expense relative to variable rate interest flows. The Group seeks to "match" interest rate risk on either side of the Statement of Financial Position. However, this is not a perfect match and interest rate risk is present on: Money market transactions of a fixed rate nature, fixed rate loans and fixed rate savings accounts. There is interest rate mismatch in Arbuthnot Latham and Secure Trust Bank. This is monitored on a daily basis in conjunction with liquidity and capital. The interest rate mismatch is daily monitored, throughout the maturity bandings of the book on a parallel shift scenario for 50, 100 and 200 basis points movement. The Group consider the 50, 100 and 200 basis points movement to be appropriate for scenario testing given the current economic outlook and industry expectations. This typically results in a pre-tax mismatch of £0.5m to £1.8m (2012: £0.6m to £2.4m) for the Group, with the same impact to equity pre-tax. The Company has no fixed rate exposures, but a upward change of 50 basis points on variable rates would increase pre-tax profits and equity by £12,000 (2012: decrease pre-tax profits and equity by £37,000).

(d) Liquidity risk

The current Liquidity regime came into force on the 1 October 2010. The PRA requires a firm to maintain at all times liquidity resources which are adequate, both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met as they fall due. There is also a requirement that a firm ensures its liquidity resources contain an adequate buffer of high quality, unencumbered assets (i.e. Government securities in the liquidity asset buffer); and it maintains a prudent funding profile. The liquid assets buffer is a pool of highly liquid assets that can be called upon to create sufficient liquidity to meet liabilities on demand, particularly in a period of liquidity stress. The liquidity resources outside the buffer must either be marketable assets with a demonstrable secondary market that the firm can access, or a credit facility that can be activated in times of stress.

The banking entities both prepared and approved their Individual Liquidity Adequacy Assessment ("ILAA"). The liquidity buffers required by the ILAA have all been put in place and maintained since. Liquidity resources outside of the buffer are made up of certificates of deposit and fixed rate notes (debt securities). The Company and Group also maintain long-term committed bank facilities.

The table below analyses the contractual undiscounted cash flows for the Group into relevant maturity groupings at 31 December 2013:

At 31 December 2013	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Non-derivative liabilities						
Deposits from banks	2,003	(2,003)	(2,003)	-	-	-
Deposits from customers	957,791	(1,013,314)	(435,868)	(388,573)	(185,953)	(2,920)
Other liabilities	10,152	(8,892)	(7,857)	(1,025)	(10)	-
Debt securities in issue	12,232	(14,224)	(100)	(299)	(1,593)	(12,232)
Issued financial guarantee contracts		(805)	(805)	-	-	-
Unrecognised loan commitments		(37,094)	(37,094)	-	-	-
	982,178	**(1,076,332)**	**(483,727)**	**(389,897)**	**(187,556)**	**(15,152)**
Derivative liabilities						
Risk management:	371	-	-	-	-	-
- Outflows		(371)	(371)	-	-	-
	371	**(371)**	**(371)**	**-**	**-**	**-**

The table below analyses the contractual undiscounted cash flows for the Group into relevant maturity groupings at 31 December 2012:

At 31 December 2012	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Non-derivative liabilities						
Deposits from banks	373	(373)	(373)	-	-	-
Deposits from customers	894,545	(916,708)	(396,331)	(364,647)	(153,320)	(2,410)
Other liabilities	23,021	(23,409)	(23,056)	(207)	(146)	-
Debt securities in issue	11,980	(13,933)	(98)	(293)	(1,562)	(11,980)
Issued financial guarantee contracts		(879)	(879)	-	-	-
Unrecognised loan commitments		(21,491)	(21,491)	-	-	-
	929,919	**(976,793)**	**(442,228)**	**(365,147)**	**(155,028)**	**(14,390)**
Derivative liabilities						
Risk management:	462	-	-	-	-	-
- Outflows		(462)	(462)	-	-	-
	462	**(462)**	**(462)**	**-**	**-**	**-**

The table below analyses the contractual undiscounted cash flows for the Company into relevant maturity groupings at 31 December 2013:

At 31 December 2013	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Non-derivative liabilities						
Bank overdraft	2,000	(2,000)	(2,000)	-	-	-
Other liabilities	7,768	(7,768)	(5,143)	(1,025)	(10)	(1,590)
Debt securities in issue	12,232	(14,224)	(100)	(299)	(1,593)	(12,232)
Issued financial guarantee contracts		(2,500)	(2,500)	-	-	-
	22,000	**(26,492)**	**(9,743)**	**(1,324)**	**(1,603)**	**(13,822)**

The table below analyses the contractual undiscounted cash flows for the Company into relevant maturity groupings at 31 December 2012:

At 31 December 2012	Carrying amount £000	Gross nominal inflow/ (outflow) £000	Not more than 3 months £000	More than 3 months but less than 1 year £000	More than 1 year but less than 5 years £000	More than 5 years £000
Non-derivative liabilities						
Due to subsidiary undertakings - bank overdraft	100	(100)	(100)	-	-	-
Other liabilities	5,552	(5,552)	(4,639)	(913)	-	-
Debt securities in issue	11,980	(13,933)	(98)	(293)	(1,562)	(11,980)
Issued financial guarantee contracts		(2,500)	(2,500)	-	-	-
	17,632	**(22,085)**	**(7,337)**	**(1,206)**	**(1,562)**	**(11,980)**

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature are important factors in assessing the liquidity of the Group and its exposure to changes in interest rates and exchange rates.

Fiduciary activities

The Group provides investment management and advisory services to third parties, which involve the Group making allocation and purchase and sale decisions in relation to a wide range of financial instruments. Those assets that are held in a fiduciary capacity are not included in these financial statements. These services give rise to the risk that the Group may be accused of maladministration or

underperformance. At the balance sheet date, the Group had investment management accounts amounting to approximately £528m (2012: £377m). Additionally the Group provides investment advisory services.

(e) Financial assets and liabilities

The tables below set out the Group's financial assets and financial liabilities into the respective classifications:

At 31 December 2013	Fair value through profit or loss £000	Held-to-maturity £000	Loans and receivables £000	Available-for-sale £000	Other amortised cost £000	Total carrying amount £000	Fair value £000
ASSETS							
Cash	-	-	193,046	-	-	193,046	193,046
Derivative financial instruments	508	-	-	-	-	508	508
Loans and advances to banks	-	-	105,061	-	-	105,061	105,061
Loans and advances to customers	-	-	732,009	-	-	732,009	730,706
Debt securities held-to-maturity	-	19,466	-	-	-	19,466	19,547
Financial investments	152	-	-	1,823	-	1,975	1,975
	660	**19,466**	**1,030,116**	**1,823**	**-**	**1,052,065**	**1,050,843**
LIABILITIES							
Deposits from banks	-	-	-	-	2,003	2,003	2,003
Derivative financial instruments	371	-	-	-	-	371	371
Deposits from customers	-	-	-	-	957,791	957,791	957,791
Debt securities in issue	-	-	-	-	12,232	12,232	12,232
	371	**-**	**-**	**-**	**972,026**	**972,397**	**972,397**

At 31 December 2012	Fair value through profit or loss £000	Held-to-maturity £000	Loans and receivables £000	Available-for-sale £000	Other amortised cost £000	Total carrying amount £000	Fair value £000
ASSETS							
Cash	-	-	203,683	-	-	203,683	203,683
Derivative financial instruments	648	-	-	-	-	648	648
Loans and advances to banks	-	-	144,391	-	-	144,391	144,391
Loans and advances to customers	-	-	586,968	-	-	586,968	585,924
Debt securities held-to-maturity	-	13,526	-	-	-	13,526	13,623
Financial investments	169	-	-	3,088	-	3,257	3,257
	817	**13,526**	**935,042**	**3,088**	**-**	**952,473**	**951,526**
LIABILITIES							
Deposits from banks	-	-	-	-	373	373	373
Derivative financial instruments	462	-	-	-	-	462	462
Deposits from customers	-	-	-	-	894,545	894,545	894,545
Debt securities in issue	-	-	-	-	11,980	11,980	11,980
	462	**-**	**-**	**-**	**906,898**	**907,360**	**907,360**

Cash, loans and advances to banks, debt securities held-to-maturity, deposits from banks and deposits from customers are classified as level 2 financial instruments, on the basis that they are liquid but not traded in an active market. Loans and advances to customers and debt securities in issue are classified as level 3 as there is no observable market data for these instruments.

7. Capital management

The Group’s capital management policy is focused on optimising shareholder value. There is a clear focus on delivering organic growth and ensuring capital resources are sufficient to support planned levels of growth. The Board regularly reviews the capital position.

In accordance with the EU's Capital Requirements Directive (CRD) and the required parameters set out in the Prudential Regulatory Authority (‘PRA’) Handbook (BIPRU 2.2), the Individual Capital Adequacy Assessment Process (ICAAP) is embedded in the risk management framework of the Group and is subject to ongoing updates and revisions when necessary. However, at a minimum, the ICAAP is updated annually as part of the business planning process. The ICAAP is a process that brings together management framework (i.e. the policies, procedures, strategies, and systems that the Group has implemented to identify, manage and mitigate its risks) and the financial disciplines of business planning and capital management. The Group's regulated entities are also the principal trading subsidiaries as detailed in note 42.

Not all material risks can be mitigated by capital, but where capital is appropriate the Board has adopted a “Pillar 1 plus” approach to determine the level of capital the Group needs to hold. This method takes the Pillar 1 capital formula calculations (standardised approach for credit, market and operational risk) as a starting point, and then considers whether each of the calculations delivers a sufficient capital sum adequately to cover management’s anticipated risks. Where the Board considered that the Pillar 1 calculations did not reflect the risk, an additional capital add-on in Pillar 2 is applied, as per the Individual Capital Guidance (ICG) issued by the PRA.

The Group's regulatory capital is divided into two tiers:

- Tier 1 comprises mainly shareholders’ funds, non-controlling interests, after deducting goodwill and other intangible assets.
- Lower Tier 2 comprises qualifying subordinated loan capital, collective provisions and revaluation reserves. Lower Tier 2 capital cannot exceed 50% of tier 1 capital.

The following table shows the regulatory capital resources as managed by the Group:

	2013 £000	2012 £000
Tier 1		
Share capital	153	153
Retained earnings	67,901	53,372
Other reserves	(1,111)	(1,393)
Non-controlling interests	20,327	16,376
Goodwill	(2,695)	(1,991)
Deductions for other intangibles	(8,710)	(5,318)
Total tier 1 capital	**75,865**	**61,199**
Tier 2		
Revaluation reserve	22	140
Collective provisions	1,578	-
Debt securities in issue	12,232	11,980
Total tier 2 capital	**13,832**	**12,120**
Total tier 1 & tier 2 capital	**89,697**	**73,319**

The ICAAP includes a summary of the capital required to mitigate the identified risks in its regulated entities and the amount of capital that the Group has available. The PRA sets ICG for each UK bank calibrated by references to its Capital Resources Requirement, broadly equivalent to 8 percent of risk weighted assets and thus representing the capital required under Pillar 1 of the Basel II framework. The ICAAP is a key input into the PRA's ICG setting process, which addresses the requirements of Pillar 2 of the Basel II framework. The PRA's approach is to monitor the available capital resources in relation to the ICG requirement. Each entity maintains an extra internal buffer and capital ratios are reviewed on a monthly basis to ensure that external requirements are adhered to. All regulated entities have complied with all of the externally imposed capital requirements to which they are subject.

In June 2013, the PRA published a final regulation to give effect to the Basel III framework, which amends the definition of Tier 1 capital. This comes into effect on 1 January 2014. The Group’s current capital position is sufficient to meet the Tier 1 capital ratio based on the Tier 1 capital definition under the new regulation.

Pillar 3 complements the minimum capital requirements (Pillar 1) and the supervisory review process (Pillar 2). Its aim is to encourage market discipline by developing a set of disclosure requirements which will allow market participants to assess key pieces of information on a firm's capital, risk exposures and risk assessment processes. Our Pillar 3 disclosures for the year ended 31

December 2013 are published as a separate document on the Group website under Investor Relations (Announcements & Shareholder Info).

8. Fee and commission income

	2013	2012
	£000	£000
Banking commissions	4,714	5,872
Trust and other fiduciary fee income	4,320	3,349
Financial Planning fees and commissions	1,351	1,149
Structured product commissions	1,810	2,441
Other fee income *	19,621	11,305
	31,816	**24,116**

* This mainly includes fee and commission income received on OneBill, PPI insurance and commission earned on debt recovery activities at Secure Trust Bank.

9. Net impairment loss on financial assets

	2013	2012
	£000	£000
Net Impairment losses on loans and advances to customers	17,734	10,984
Impairment losses on financial investments	1,073	-
	18,807	**10,984**

10. Gain from a bargain purchase

On 15 January 2013 Debt Managers (Services) Limited (DMS), a wholly owned subsidiary of Secure Trust Bank, acquired certain trade and assets from Debt Managers Holdings Ltd, Debt Managers (AB) Limited and Debt Managers Limited (together "Debt Managers"). Debt Managers collects debt on behalf of a range of clients including banks and utility companies.

Key benefits of this acquisition to Secure Trust Bank include:
• Broadening the income base of Secure Trust Bank without the requirement for large amounts of capital;
• The acquisition of a scalable collections platform through which Secure Trust Bank intends to channel its delinquent debt; and
• The acquisition of the latest call centre and collections technology, including market leading dialler capability, interactive voice response technology and payment websites.

DMS acquired the Debt Managers business for an initial cash payment of £0.4 million paid on completion of the transaction. Deferred consideration of up to £0.3 million was payable by DMS one year after completion subject to the business achieving certain performance criteria. Of this, £0.1 million was paid by DMS in final settlement.

The acquired assets included a software platform jointly developed with a third party. Upon completion the rights to this software were sold to that third party for consideration of £2 million. DMS then proceeded to lease back the internal rights to use this software. On completion Secure Trust Bank provided DMS with £2.2 million of funding to clear an outstanding overdraft of £1.8 million and to fund the working capital requirements of DMS.

The Consolidated Statement of Comprehensive Income includes revenue of £3.8 million and a loss before tax of £0.9 million attributable to DMS. Had the acquisition occurred at the start of the financial year, the Consolidated Statement of Comprehensive Income would have included revenue of £4.0 million and a loss before tax of £0.9 million attributable to DMS.

	Acquired assets / liabilities	Fair value adjustments	Recognised values on acquisition
	£000	£000	£000
Clients cash at bank	1,362	-	1,362
Other assets	1,117	263	1,380
Intangible assets	2,010	-	2,010
Property, plant and equipment	57	-	57
Total assets	**4,546**	**263**	**4,809**

Bank overdraft	1,846	-	1,846
Client account	1,301	-	1,301
Other liabilities	730	-	730
Total liabilities	**3,877**	**-**	**3,877**
Net identifiable (liabilities)/assets	**669**	**263**	**932**
Consideration			519
Goodwill			**(413)**

On 8 June 2012 Secure Trust Bank PLC ("STB") acquired 100% of the shares in Everyday Loans Holdings Limited and its wholly owned subsidiaries Everyday Loans Limited and Everyday Lending Limited (together "ELL"). STB acquired ELL for consideration of £1. Upon acquisition STB provided funding so that ELL could redeem the remaining £34 million of subordinated debt and also provided a loan facility of £37 million to refinance ELL's existing bank debt and to fund future loans. A gain on acquisition of £9.8m arose from the difference between the acquisition price and the fair value of net assets acquired. This is expected to amortise through the profit and loss account over 3 to 5 years.

	Acquired assets / liabilities £000	Fair value adjustments £000	Recognised values on acquisition £000
Intangible assets	50	5,115	5,165
Property, plant and equipment	491	-	491
Loans and advances to customers	63,720	7,545	71,265
Cash at bank	991	-	991
Other assets	24	-	24
Prepayments and accrued income	2,939	-	2,939
Deferred tax asset	-	6,313	6,313
Total assets	68,215	18,973	87,188
Loans and debt securities	71,618	-	71,618
Other liabilities	960	-	960
Accruals and deferred income	1,741	-	1,741
Deferred tax liabilities	-	3,039	3,039
Total liabilities	74,319	3,039	77,358
Net identifiable (liabilities) / assets	(6,104)	15,934	9,830
Consideration - £1			-
Gain on acquisition			**9,830**

11. Gain on Sale of Building

On 17 October 2013 Arbuthnot Latham & Co., Limited completed the sale and leaseback of 7-21 Wilson Street. The net book value of the property at the date of sale was £16.5m. Under the terms of the sale and leaseback agreement, the cash consideration received by Arbuthnot Latham was £26.2m paid on completion. The Buyer is also providing £5.4m to be drawn by Arbuthnot Latham to fund a renovation and fit out programme. After providing £3.0 million for the rent payable during the period of refurbishment prior to occupation and £0.2m of transaction costs, the net gain was £6.5m.

12. Disposals

On 20 March 2012 Arbuthnot Banking Group PLC agreed terms for the sale of Arbuthnot AG. The company was sold to Ducartis Holding AG for a total cash consideration of CHF 2.0m (£1.4m) which resulted in a profit for the Group of £0.8m.

13. Other income

Arbuthnot Latham received £1.2m of rental income in the year from the letting of the 7-21 Wilson Street property. The property was vacated by the tenants at the end of September 2013 and refurbishment works started soon afterwards in anticipation of the Group occupation of the building in 2015.

Up to the date of sale of Arbuthnot AG, the purchaser funded most of the running costs for this entity, which is included in other income and amounted to £nil (2012: £0.3m). In Secure Trust Bank there was also some other sundry income amounting to £nil (2012: £0.1m).

14. Discontinued operations

On 20 January 2012 the Group completed the sale of Arbuthnot Securities Limited resulting in an after tax loss of £0.3m.

15. Operating expenses

Operating expenses comprise:	2013 £000	2012 £000
Staff costs, including Directors:		
Wages and salaries	33,262	25,016
Social security costs	3,553	2,686
Pension costs	1,509	1,084
Share based payment transactions (note 38)	2,249	1,610
Amortisation of intangibles (note 29)	2,803	1,062
Depreciation (note 30)	1,015	899
Operating lease rentals	4,617	2,463
Costs arising from acquisitions	535	1,397
Other administrative expenses	24,088	16,826
Total operating expenses	**73,631**	**53,043**

Remuneration of the auditor and its associates, excluding VAT, was as follows:	2013 £000	2012 £000
Fees payable to the Company's auditor for the audit of the Company's annual accounts	82	82
Fees payable to the Company's auditor and its associates for other services:		
Audit of the accounts of subsidiaries	356	263
Audit related assurance services	104	104
Taxation compliance services	73	178
Taxation advisory services	62	48
Other assurance services	56	-
Corporate finance services	-	250
Other non-audit services	28	47
Total fees payable	**761**	**972**

Remuneration for corporate finance services in 2012 include £250,000 in relation to the acquisition of Everyday Loans Holdings Limited.

Audit related assurance services include regulatory audits and interim profit verifications. Other non-audit services include fees for ad hoc accounting advice.

16. Average number of employees

	2013	2012
Retail banking	530	399
Private banking	145	144
Group	16	16
	691	**559**

17. Income tax expense

	2013	2012

United Kingdom corporation tax at 23.25% (2012: 24.5%)	£000	£000
Current taxation		
Corporation tax charge - current year	3,146	1,068
Corporation tax charge - adjustments in respect of prior years	548	481
	3,694	**1,549**
Deferred taxation		
Origination and reversal of temporary differences	1,006	(297)
Adjustments in respect of prior years	(502)	(124)
	504	**(421)**
Income tax expense	**4,198**	**1,128**
Tax reconciliation		
Profit before tax	15,713	12,593
Tax at 23.25% (2012: 24.5%)	3,653	3,085
Permanent differences	208	(2,573)
Tax rate change	291	259
Prior period adjustments	46	357
Corporation tax charge for the year	**4,198**	**1,128**

Of the £2,573,000 permanent differences in 2012, £2,408,000 relates to the non-taxable gain from a bargain purchase.

The UK corporation tax rate reduced from 26% to 24% with effect from 1 April 2012, to 23% with effect from 1 April 2013 and to 21% from 1 April 2014. On 2 July 2013 the Government substantively enacted a further reduction to the UK corporation tax rate to 20% from 1 April 2015. This will reduce the Company's future current tax charge accordingly.

18. Earnings per ordinary share

Basic and fully diluted

Earnings per ordinary share are calculated by dividing the profit after tax attributable to equity holders of the Company of £7,930,000 (2012: £8,041,000) by the weighted average number of ordinary shares 15,279,322 (2012: 15,279,322) in issue during the year. There is currently no difference between basic and fully diluted earnings per ordinary share.

19. Cash

	2013 £000	2012 £000
Cash in hand included in cash and cash equivalents (note 40)	**193,046**	**203,683**

In 2010 a reserve account was opened at the Bank of England (BoE) to comply with the new liquidity regime that came into force on 1 October 2010. Surplus funds are now mainly held in the BoE reserve account, with the remainder held in certificates of deposit, fixed rate notes and money market deposits in highly rated banks (the majority held in UK clearing banks).

20. Loans and advances to banks

	2013 £000	2012 £000
Placements with banks included in cash and cash equivalents (note 40)	**105,061**	**144,391**

The table below presents an analysis of loans and advances to banks by rating agency designation as at 31 December, based on Moody's long term ratings:

	2013 £000	2012 £000
Aaa	57,101	68,783
Aa3	-	23,082
A1	-	13,373
A2	44,327	39,153
A3	3,633	-

	105,061	**144,391**

None of the loans and advances to banks is either past due or impaired.

21. Debt securities held-to-maturity

Debt securities represent certificates of deposit. The Group's intention is to hold them to maturity and, therefore, they are stated in the Statement of Financial Position at amortised cost.

The movement in debt securities held to maturity may be summarised as follows:	2013 £000	2012 £000
At 1 January	13,526	40,079
Additions	9,844	51,012
Redemptions	(3,904)	(77,565)
At 31 December	**19,466**	**13,526**

The table below presents an analysis of debt securities by rating agency designation at 31 December, based on Moody's long term ratings:

	2013 £000	2012 £000
Aaa	14,120	8,026
Aa1	3,044	-
Aa3	2,302	1,500
A3	-	4,000
	19,466	**13,526**

None of the debt securities held-to-maturity is either past due or impaired.

22. Derivative financial instruments

	2013			2012		
	Contract/ notional amount £000	Fair value assets £000	Fair value liabilities £000	Contract/ notional amount £000	Fair value assets £000	Fair value liabilities £000
Currency swaps	39,850	488	371	41,206	623	462
Interest rate caps	20,000	20	-	20,000	25	-
	59,850	**508**	**371**	**61,206**	**648**	**462**

The principal derivatives used by the Group are exchange rate contracts and interest rate caps (used for cash flow hedges). Exchange rate related contracts include currency swaps and cash flow hedges include interest rate caps.

A forward foreign exchange contract is an agreement to buy or sell a specified amount of foreign currency on a specified future date at an agreed rate. Currency swaps generally involve the exchange of interest payment obligations denominated in different currencies; exchange of principal can be notional or actual. The currency swaps are settled net and therefore the fair value is small in comparison to the contract/notional amount.

An interest rate cap is an option contract which puts an upper limit on a floating exchange rate. The writer of the cap has to pay the holder of the cap the difference between the floating rate and the reference rate when that reference rate is breached. The holder pays a premium for the cap.

Also included in derivative financial instruments are structured notes not yet placed to investors. These notes contain embedded derivatives (embedded options to buy and sell indicies) and non-derivative host contracts (discounted bonds). Both the host and embedded derivatives are presented net within derivative financial instruments.

The Group only uses investment graded banks as counterparties for derivative financial instruments.

The table below presents an analysis of derivative financial instruments contract/notional amounts by rating agency designation of counterparty bank at 31 December, based on Moody's long term ratings:

	2013	2012
	£000	£000
Aa3	39,850	41,206
A1	20,000	20,000
	59,850	**61,206**

23. Loans and advances to customers

	2013	2012
	£000	£000
Gross loans and advances	763,042	607,616
Less: allowances for impairment on loans and advances (note 24)	(31,033)	(20,648)
	732,009	**586,968**

For a maturity profile of loans and advances to customers, refer to note 6.

	2013	2012
Loans and advances to customers include finance lease receivables as follows:	£000	£000
Gross investment in finance lease receivables:		
- No later than 1 year	16,386	22,188
- Later than 1 year and no later than 5 years	16,053	13,047
	32,439	35,235
Unearned future finance income on finance leases	(6,885)	(8,914)
Net investment in finance leases	**25,554**	**26,321**
The net investment in finance leases may be analysed as follows:		
- No later than 1 year	12,905	10,509
- Later than 1 year and no later than 5 years	12,649	15,812
	25,554	**26,321**

	2013	2012
Loans and advances to customers can be further summarised as follows:	£000	£000
Neither past due nor impaired	684,783	550,640
Past due but not impaired	19,210	14,756
Impaired	59,049	42,220
Gross	763,042	607,616
Less: allowance for impairment	(31,033)	(20,648)
Net	**732,009**	**586,968**

(a) Loans and advances past due but not impaired

	2013	2012
Gross amounts of loans and advances to customers that were past due but not impaired were as follows:	£000	£000
Past due up to 30 days	2,681	1,160
Past due 30 - 60 days	4,369	4,584
Past due 60 - 90 days	3,439	5,354
Over 90 days	8,721	3,658
Total	**19,210**	**14,756**

Loans and advances normally fall into this category when there is a delay in either the sale of the underlying collateral or the completion of formalities to extend the credit facilities for a further period. Management have no material concerns regarding the quality of the collateral that secures the lending.

(b) Loans and advances renegotiated

Restructuring activities include external payment arrangements, modification and deferral of payments. Following restructuring, a previously overdue customer account is reset to a normal status and managed together with other similar accounts. Restructuring policies and practices are based on indicators or criteria which, in the judgement of management, indicate that payment will most likely continue. These policies are kept under continuous review. Renegotiated loans that would otherwise be past due or impaired totalled £nil (2012: £nil).

(c) Collateral held

An analysis of loans and advances to customers past due or impaired by reference to the fair value of the underlying collateral is as follows:

	2013	2012
	£000	£000
Past due but not impaired	62,168	39,162
Impaired	10,963	7,881
Fair value of collateral held	**73,131**	**47,043**

Collateral is shown at fair value less costs to sell. The fair value of the collateral held is £73,131,000 against £47,226,000 secured loans, giving an average loan-to-value of 65% (2012: 77%).

The gross amount of individually impaired loans and advances to customers before taking into account the cash flows from collateral held is £28,016,000 (2012: £21,572,000).

Interest income on loans classified as impaired totalled £2,574,000 (2012: £1,601,000).

24. Allowances for impairment of loans and advances

	2013	2012
Reconciliation of specific allowance for impairments:	£000	£000
At 1 January	20,278	11,250
Impairment losses	17,590	11,248
Loans written off during the year as uncollectible	(8,413)	(1,586)
Amounts recovered during the year	-	(634)
At 31 December	**29,455**	**20,278**

	2013	2012
Reconciliation of collective allowance for impairments:	£000	£000
At 1 January	370	-
Impairment losses	1,208	370
At 31 December	**1,578**	**370**

	2013	2012
A further analysis of allowances for impairment of loans and advances is as follows:	£000	£000
Loans and advances to customers - UK Private Bank	3,973	4,423
Loan and advances to customers - Retail Bank - unsecured	27,060	16,225
At 31 December	**31,033**	**20,648**

25. Other assets

Group	2013 £000	2012 £000
Trade receivables	6,135	3,393
Repossessed collateral - held as inventory	3,543	2,586
Prepayments and accrued income	7,589	5,687
	17,267	**11,666**

Land acquired through repossession of collateral which is subsequently held in the ordinary course of business with a view to develop and sell is accounted for as inventory.

Company	2013 £000	2012 £000
Trade receivables	731	731
Due from subsidiary undertakings	4,579	4,578
Prepayments and accrued income	105	353
	5,415	**5,662**

26. Financial investments

Group:	2013 £000	2012 £000
Financial investments comprise:		
- Securities (at fair value through profit and loss)	152	169
- Securities (available-for-sale)	1,823	3,088
Total financial investments	**1,975**	**3,257**

Unlisted securities
The Group has made equity investments in unlisted special purpose vehicles set up to acquire and enhance the value of commercial properties. These investments are of a medium term nature. There is no open market for these investments therefore the Group has valued them using appropriate valuation methodologies, which include net asset valuations and discounted future cash flows.

The Directors intend to dispose of these assets when a suitable buyer has been identified and when the Directors believe that the underlying assets have reached their maximum value.

Company	2013 £000	2012 £000
Financial investments comprise:		
- Securities (at fair value through profit and loss)	152	169
- Securities (available-for-sale)	13	244
Total financial investments	165	413

27. Deferred taxation

The deferred tax asset comprises:

	2013 £000	2012 £000
Unrealised surplus on revaluation of freehold property	173	(71)
Accelerated capital allowances and other short-term timing differences	(160)	(673)
Fair value of derivatives	100	110
Tax losses	2,742	5,057
Deferred tax asset	**2,855**	**4,423**
At 1 January	4,423	629
On acquisition of V12/ELL	(960)	3,276
Revaluation reserve	242	-

Profit and loss account - accelerated capital allowances and other short-term timing differences	589	1,040
Profit and loss account - tax losses	(1,439)	(522)
Deferred tax asset at 31 December	**2,855**	**4,423**

The above balance is made up as follows:

	2013 £000	2012 £000
Deferred tax assets within the Group	3,954	5,057
Deferred tax liabilities within the Group	(1,099)	(634)
	2,855	**4,423**

Deferred tax assets are recognised for tax losses to the extent that the realisation of the related tax benefit through future taxable profits is probable.

The UK corporation tax rate reduced from 26% to 24% with effect from 1 April 2012, to 23% with effect from 1 April 2013 and to 21% with effect from 1 April 2014. This will reduce the Group's future current tax charge accordingly. Deferred tax has been calculated based on a rate of 21% to the extent that the related temporary or timing differences are expected to reverse.

On 2 July 2013 the Government substantively enacted a further reduction to the UK corporation tax rate to 20% from 1 April 2015. It has not yet been possible to quantify the full anticipated effect of the announced further 1% reduction, although this will further reduce the Group's future tax charge and reduce the Group's deferred tax assets and liabilities accordingly.

28. Investment in associate

	2013 £000	2012 £000
Investment in associate	**943**	**-**

On 11 October 2013, Arbuthnot Latham & Co. together with Praxis (Holding) Limited, formed a special purpose vehicle in the form of a separate legal entity (Tarn Crag Limited). The purpose of this legal entity is to refurbish and re-let a property in Glasgow, with the intention to exit via a sale to an institutional investor in circa 5 years time. The investment is accounted for using the equity method.

No profit or loss was recorded in the current year. The summarised financial information of the associate is set out below:

At 31 December 2013	£000
ASSETS	
Cash	320
Property, plant and equipment	10,580
	10,900
LIABILITIES	
Bank loans	9,500
Debt securities in issue	1,400
	10,900

29. Intangible assets

Group	Goodwill £000	Computer software £000	Other intangibles £000	Total £000
Cost				
At 1 January 2012	1,991	4,920	-	6,911
Additions	-	662	-	662
On acquisition of ELL (note 11)	-	50	5,115	5,165
At 31 December 2012	**1,991**	**5,632**	**5,115**	**12,738**

Additions	-	948	214	1,162
On acquisition of V12 & DMS (note 11 and 44)	704	5,414	2,200	8,318
Disposals	-	(1,900)	-	(1,900)
At 31 December 2013	**2,695**	**10,094**	**7,529**	**20,318**
Accumulated amortisation				
At 1 January 2012	-	(3,350)	-	(3,350)
Amortisation charge	-	(367)	(695)	(1,062)
At 31 December 2012	**-**	**(3,717)**	**(695)**	**(4,412)**
Amortisation charge	-	(1,307)	(1,496)	(2,803)
At 31 December 2013	**-**	**(5,024)**	**(2,191)**	**(7,215)**
Net book amount				
At 31 December 2012	1,991	1,915	4,420	8,326
At 31 December 2013	2,695	5,070	5,338	13,103

Company	Computer software £000
Cost	
At 1 January 2012	40
At 31 December 2012	**40**
At 31 December 2013	**40**
Accumulated amortisation	
At 1 January 2012	(12)
Amortisation charge	(8)
At 31 December 2012	**(20)**
Amortisation charge	(8)
At 31 December 2013	**(28)**
Net book amount	
At 31 December 2012	20
At 31 December 2013	12

Refer to note 4.2 for assumptions used in the impairment review of goodwill.

30. Property, plant and equipment

Group	Freehold land and buildings £000	Leasehold improvements £000	Computer and other equipment £000	Total £000
Cost or valuation				
At 1 January 2012	4,850	-	11,174	16,024
Additions	16,789	5	818	17,612
On acquisition of ELL (note 11)	-	540	-	540
Disposals	-	(32)	(200)	(232)
At 31 December 2012	**21,639**	**513**	**11,792**	**33,944**
Additions	-	122	624	746
On acquisition of V12 & DMS (note 11 and 44)	-	9	78	87
Disposals	(16,789)	(16)	(461)	(17,266)
At 31 December 2013	**4,850**	**628**	**12,033**	**17,511**

Accumulated depreciation				
At 1 January 2012	(685)	-	(10,125)	(10,810)
Depreciation charge	(199)	(101)	(567)	(867)
Disposals	-	22	198	220
At 31 December 2012	**(884)**	**(79)**	**(10,494)**	**(11,457)**
Depreciation charge	(301)	(168)	(546)	(1,015)
Disposals	345	-	138	483
At 31 December 2013	**(840)**	**(247)**	**(10,902)**	**(11,989)**
Net book amount				
At 31 December 2012	**20,755**	**434**	**1,298**	**22,487**
At 31 December 2013	**4,010**	**381**	**1,131**	**5,522**

The Group's freehold property at 1 Arleston Way, Solihull, B90 4LH, was valued on 17 December 2008 by an Independent external valuer, who is a Fellow of the Royal Institution of Chartered Surveyors. The Valuation was in accordance with the requirements of the RICS Valuation Standards 6th Edition and the International Valuation Standards. The Valuation of the property was on the basis and assumption it is an Owner/Occupied property, valued to Market Value assuming that the property will be sold as part of the continuing business. The Valuer's opinion of Market Value was primarily derived using comparable recent market transactions on arms-length terms. The Directors have assessed the value at year end through comparison to current rental yields on similar properties in the area and do not believe that the fair value of freehold property is materially different from the carrying value.

On 3 August 2012 the Group acquired freehold premises at 7-21 Wilson Street, London, EC2M 2TD (“Wilson Street”) for £15.7 million plus acquisition costs (including stamp duty) of £1.1m. On 17 October 2013 the Group disposed of the property and leased it back from the purchaser.

The carrying value of freehold land not depreciated is £0.5 million (2012: £1.7 million). The historical cost of freehold property included at valuation is as follows:

	2013 £000	2012 £000
Cost	4,832	20,567
Accumulated depreciation	(1,063)	(1,102)
Net book amount	**3,769**	**19,465**

Company	Computer and other equipment £000
Cost or valuation	
At 1 January 2012	189
Additions	13
At 31 December 2012	**202**
Additions	1
At 31 December 2013	**203**
Accumulated depreciation	
At 1 January 2012	(62)
Depreciation charge	(6)
At 31 December 2012	**(68)**
Depreciation charge	(5)
At 31 December 2013	**(73)**

Net book amount	
At 31 December 2012	**134**
At 31 December 2013	**130**

31. Deposits from banks

	2013	2012
	£000	£000
Deposits from other banks	**2,003**	**373**

For a maturity profile of deposits from banks, refer to Note 6.

32. Deposits from customers

	2013	2012
	£000	£000
Current/demand accounts	366,797	260,037
Term deposits	590,994	634,508
	957,791	**894,545**

Included in customer accounts are deposits of £9,947,000 (2012: £8,578,000) held as collateral for loans and advances. The fair value of these deposits approximates the carrying value.

For a maturity profile of deposits from customers, refer to Note 6.

33. Other liabilities

	2013	2012
Group	£000	£000
Trade payables	10,152	7,656
Accruals and deferred income	20,865	15,365
	31,017	**23,021**

The Financial Services Compensation Scheme ('FSCS') has provided compensation to consumers following the collapse of a number of deposit takers. The compensation paid out to consumers is currently funded through loans from the Bank of England and HM Treasury.

In previous years the Company has applied a trigger date for recognition of FSCS liabilities of 31 December. During 2013 this was changed to 1 April.

Included in accruals is a provision for non occupancy rent of £3m (2012: £nil). This was taken into account when calculating the profit on the sale and leaseback of the Wilson Street property (see note 11).

Company	£000	£000
Due to subsidiary undertakings	7,768	4,639
Accruals and deferred income	1,261	913
	9,029	**5,552**

34. Debt securities in issue

	2013	2012
	£000	£000
Subordinated loan notes 2035	**12,232**	**11,980**

The subordinated loan notes 2035 were issued on 7 November 2005 and are denominated in Euros. The principal amount outstanding at 31 December 2013 was €15,000,000 (2012: €15,000,000). The notes carry interest at 3% over the interbank rate for three month deposits in euros and are repayable at par in August 2035 unless redeemed or repurchased earlier by the Company.

The contractual undiscounted amount that will be required to be paid at maturity of the above debt securities is €15,000,000.

Given the fact that the Group has never been subject to a published credit rating by any of the relevant agencies and the notes in issue are not quoted, it is not considered possible to approximate a fair value for these notes.

35. Contingent liabilities and commitments

Capital commitments

At 31 December 2013, the Group had capital commitments of £nil (2012: £nil) in respect of equipment purchases.

Credit commitments

The contractual amounts of the Group's off-balance sheet financial instruments that commit it to extend credit to customers are as follows:

	2013	2012
	£000	£000
Guarantees and other contingent liabilities	805	879
Commitments to extend credit:		
- Original term to maturity of one year or less	37,094	21,491
	37,899	**22,370**

Operating lease commitments

Where a Group company is the lessee, the future aggregate lease payments under non-cancellable operating leases are as follows:

	2013	2012
	£000	£000
Expiring:		
Within 1 year	4,672	1,982
Later than 1 year and no later than 5 years	9,636	3,168
Later than 5 years	19,351	29
	33,659	**5,179**

The lease on the Group's current premises at 20 Ropemaker Street, London, EC2Y 9AR, costs £1.7 million per annum and has a break option in June 2015. The Group has exercised the break option and Wilson Street (see note 11) will become the head office for Arbuthnot Banking Group PLC, the principal location for Arbuthnot Latham & Co., Limited and London offices for Secure Trust Bank PLC. Arbuthnot entered into a 16 year lease on Wilson Street, with a break at 11 years and rent reviews after 5, 10 and 15 years. The initial rent is £1.75 million per annum. These two leases form the most significant part of the operating leases disclosed in the table above.

36. Share capital

	Number of shares	Ordinary share capital	Share premium
		£000	£000
At 1 January 2012	15,279,322	153	21,085
Cancellation of share premium account	-	-	(21,085)
At 31 December 2012 & 31 December 2013	**15,279,322**	**153**	**-**

During 2012 the share premium was cancelled and transferred to reserves.

At 31 December 2013 the Company held 390,274 shares (2012: 390,274) in treasury.

37. Reserves and retained earnings

	2013	2012
Group	£000	£000
Revaluation reserve	191	140
Capital redemption reserve	20	20
Available-for-sale reserve	(169)	81

Cash flow hedging reserve	(378)	(363)
Treasury shares	(1,131)	(1,131)
Retained earnings	67,901	53,372
Total reserves at 31 December	**66,434**	**52,119**

The revaluation reserve represents the unrealised change in the fair value of properties.

The capital redemption reserve represents a reserve created after the Company purchased its own shares which resulted in a reduction of share capital.

	2013	2012
Company	£000	£000
Capital redemption reserve	20	20
Available-for-sale reserve	81	81
Treasury shares	(1,131)	(1,131)
Retained earnings	31,325	20,768
Total reserves as 31 December	**30,295**	**19,738**

38. Share-based payment options

Company
On 16 April 2013 Mr. Salmon exercised the option granted to him on 21 May 2008 to subscribe for 100,000 ordinary 1p shares in the Company at 337.5p and Mr. Cobb exercised the option granted to him on 5 November 2008 to subscribe for 50,000 ordinary 1p shares in the Company at 320p. The exercise price was 930p per share and the Board agreed to make a cash settlement of £897k rather than allot new shares. On the same day Mr. Salmon and Mr. Cobb were granted new options and as such the Company had the following equity settled share-based payment awards outstanding at 31 December 2013:

- On 16 April 2013 Mr. Salmon was granted an option to subscribe for 100,000 ordinary 1p shares in the Company between April 2016 and April 2021 at 930p. The fair value of the option at grant date was £83k.
- On 16 April 2013 Mr. Cobb was granted an option to subscribe for 50,000 ordinary 1p shares in the Company between April 2016 and April 2021 at 930p. The fair value of the option at grant date was £41k.

There are no other vesting conditions for these awards.

Group
Apart from the share-based payment awards for the Company listed above, the Group also include awards allocated under the Secure Trust Bank Share Option Scheme, which was established on 17 October 2011 and entitles key management personnel and senior employees of Secure Trust Bank PLC to purchase shares in that company.

The performance conditions of the Scheme are that for the duration of the vesting period, the dividends paid by Secure Trust Bank PLC must have increased in percentage terms when compared to an assumed dividend of £8 million in respect of the financial year ending 31 December 2012, by a minimum of the higher of:

a) the increase in the Retail Prices Index during that period; or
b) 5% per annum during that period.

All dividends paid by Secure Trust Bank each year during the vesting period must be paid from Secure Trust Bank's earnings referable to that year. Also from the grant date to the date the Option is exercised, there must be no public criticism by any regulatory authority on the operation of Secure Trust Bank or any of its subsidiaries which has a material impact on the business of the Company.

Options are forfeited if they remain unexercised after a period of more than 10 years from the date of grant. If the participant ceases to be employed by the Group by reason of injury, disability, ill-health or redundancy; or because his employing company ceases to be a shareholder of the Group; or because his employing business is being transferred out of the Group, his option may be exercised within 6 months after such cessation. In the event of the death of a participant, the personal representatives of a participant may exercise an option, to the extent exercisable at the date of death, within 6 months after the death of the participant.

On cessation of employment for any other reason (or when a participant serves, or has been served with, notice of termination of such employment), the option will lapse although the Remuneration Committee has discretion to allow the exercise of the option for a period not exceeding 6 months from the date of such cessation.

In such circumstances, the performance conditions may be modified or waived as the Remuneration Committee, acting fairly and reasonably and taking due consideration of the circumstances, thinks fit. The number of Ordinary Shares which can be acquired on exercise will be pro-rated on a time elapsed basis, unless the Remuneration Committee, acting fairly and reasonably and taking due consideration of the circumstances, decides otherwise. In determining whether to exercise its discretion in these respects, the Remuneration Committee must satisfy itself that the early exercise of an option does not constitute a reward for failure.

On 2 November 2011 934,998 share options were granted at an exercise price of 720p per share. Half of the share options are exercisable on 2 November 2014 with the remainder exercisable on 2 November 2016, being SOS1 and SOS2 respectively. At the grant date these share options had a fair value of £1.6m. Of the share options granted on 2 November 2011, the following were to Group directors:

- Mr. Lynam was granted an option to subscribe for 141,666 ordinary 40p shares in Secure Trust Bank at 720p between 2 November 2014 and 1 November 2021 and a further 141,667 shares at 720p between 2 November 2016 and 1 November 2021.

- Mr. Salmon was granted an option to subscribe for 141,666 ordinary 40p shares in Secure Trust Bank at 720p between 2 November 2014 and 1 November 2021 and a further 141,667 shares at 720p between 2 November 2016 and 1 November 2021.

During 2013, the Share Option Scheme was changed to become an equity settled scheme without a change in fair value. The original grant date valuation was previously determined to be £1.69 per option and this valuation has been used to determine the charge for the year. An attrition rate of option holders has been assumed of 8% for the first tranche of share options and 15% for the second tranche. Also due to the options being fully conditional knockout options, a probability of pay-out has been assigned based on the likelihood of meeting the performance criteria, which is 95% and 80% respectively for the two share option tranches.

Summary details of the Secure Trust Bank Share Option Scheme are shown in the table below:

	31 December 2013			
	No.	SOS1	SOS2	Total
Key Management Personnel	3	318,750	318,749	637,499
Senior Management	5	141,666	141,666	283,332
Share Options in Issue	**8**	**460,416**	**460,415**	**920,831**
Exercise Price (£)		7.20	7.20	
Value per option (£)		1.69	1.69	
Total included in reserves (£000)		**790**	**790**	**1,580**
Behavioural assumption (attrition)		7.6%	15.2%	
Probability of payout		95%	80%	
Total (£000)		**693**	**536**	**1,229**

39. Dividends per share

Final dividends are not accounted for until they have been approved at the Annual General Meeting. At the meeting on 8 May 2014, a dividend in respect of 2013 of 15 pence per share (2012: actual dividend 14 pence per share) amounting to a total of £2.23m (2012: actual £2.08m) is to be proposed. The financial statements for the year ended 31 December 2013 do not reflect the final dividend which will be accounted for in shareholders' equity as an appropriation of retained profits in the year ending 31 December 2014.

40. Cash and cash equivalents

For the purposes of the Statement of Cash Flows, cash and cash equivalents comprises of the following balances with less than three months maturity from the date of acquisition.

	2013	2012
	£000	£000
Cash (Note 19)	193,046	203,683
Loans and advances to banks (Note 20)	105,061	144,391
	298,107	**348,074**

41. Related party transactions

Related parties of the Company and Group include subsidiaries, Key Management Personnel, close family members of Key Management Personnel and entities which are controlled, jointly controlled or significantly influenced, or for which significant voting power is held, by Key Management Personnel or their close family members.

Other than the directors' remuneration, payment of dividends and transactions with subsidiaries, there were no related party transactions within the Parent Company. A number of banking transactions are entered into with related parties in the normal course of business on normal commercial terms. These include loans and deposits. Except for the directors' disclosures, there were no other Key Management Personnel disclosures; therefore the tables below relate to directors.

	2013	2012
	£000	£000
Loans		
Loans outstanding at 1 January	2,648	2,377
Loans advanced during the year	3,160	391
Loan repayments during the year	(620)	(120)
Loans outstanding at 31 December	**5,188**	**2,648**
Interest income earned	**138**	**118**

The loans to directors are secured on property, shares or cash and bear interest at rates linked to base rate. No provisions have been recognised in respect of loans given to related parties (2012: £nil). Details of directors' remuneration are given in the Remuneration Report. The Directors do not believe that any other key management disclosures are required.

	2013	2012
	£000	£000
Deposits		
Deposits at 1 January	1,767	1,273
Deposits placed during the year	3,237	1,332
Deposits repaid during the year	(2,482)	(838)
Deposits at 31 December	**2,522**	**1,767**
Interest expense on deposits	**20**	**97**

Details of principal subsidiaries are given in Note 42. Transactions and balances with subsidiaries are shown below:

	2013		2012	
	Highest balance during the year	Balance at 31 December	Highest balance during the year	Balance at 31 December
	£000	£000	£000	£000
ASSETS				
Due from subsidiary undertakings	21,130	21,130	24,009	4,928
Shares in subsidiary undertakings	31,847	30,995	30,847	30,847
Total assets	**52,977**	**52,125**	**54,856**	**35,775**
LIABILITIES				
Due to subsidiary undertakings	8,003	7,768	10,738	4,740

Total liabilities	**8,003**	**7,768**	**10,738**	**4,740**
Issued guarantee contracts	2,500	2,500	2,500	2,500

The disclosure of the year-end balance and the highest balance during the year is considered the most meaningful information to represent the transactions during the year. The above transactions arose during the normal course of business and are on substantially the same terms as for comparable transactions with third-parties.

42. Investment in subsidiary undertakings

Arbuthnot Banking Group PLC:	Investment at cost £000	Impairment provisions £000	Net £000
At 1 January 2012	31,515	(6,282)	25,233
Sale of Arbuthnot Securities Limited	(4,062)	3,718	(344)
Sale of Arbuthnot AG	(42)	-	(42)
Capital contribution in Arbuthnot Latham & Co., Limited	1,000	-	1,000
Allotment of shares in Secure Trust Bank PLC	5,000	-	5,000
At 31 December 2012	**33,411**	**(2,564)**	**30,847**
Capital contribution in Arbuthnot Latham & Co., Limited	1,000	-	1,000
Sale of shares in Secure Trust Bank PLC	(852)	-	(852)
At 31 December 2013	**33,559**	**(2,564)**	**30,995**

	2013 £000	2012 £000
Subsidiary undertakings:		
Banks	28,547	28,547
Other	2,448	2,300
Total	**30,995**	**30,847**

The principal subsidiary undertakings of Arbuthnot Banking Group PLC at 31 December 2013 were:

	Country of incorporation	Interest %	Principal activity
Secure Trust Bank PLC	UK	67	Retail banking
Arbuthnot Latham & Co., Limited	UK	100	Private banking

(i) All the above subsidiary undertakings are included in the consolidated financial statements and have an accounting reference date of 31 December.

(ii) All the above interests relate wholly to ordinary shares.

43. Operating segments

The Group is organised into three main operating segments, arranged over two separate companies with each having its own specialised banking service, as disclosed below:

1) Retail banking — incorporating household cash management, personal lending and banking and insurance services.
2) UK Private banking — incorporating private banking and wealth management.
3) Group Centre – ABG Group Centre management

Transactions between the operating segments are on normal commercial terms. Centrally incurred expenses are charged to operating segments on an appropriate pro-rata basis. Segment assets and liabilities comprise operating assets and liabilities, being the majority of the balance sheet.

Continuing operations			
Retail banking	UK Private banking	Group Centre	**Total**

Year ended 31 December 2013	£000	£000	£000	£000
Interest revenue	73,790	19,712	101	**93,603**
Inter-segment revenue	(62)	(209)	(3)	**(274)**
Interest revenue from external customers	73,728	19,503	98	**93,329**
Fee and commission income	22,745	9,071	-	**31,816**
Revenue from external customers	**96,473**	**28,574**	**98**	**125,145**
Interest expense	(12,905)	(6,934)	(22)	**(19,861)**
Subordinated loan note interest	-	-	(418)	**(418)**
Fee and commission expense	(4,648)	(198)	-	**(4,846)**
Segment operating income	78,982	21,651	(613)	**100,020**
Impairment losses	(15,644)	(2,914)	(249)	**(18,807)**
Gain from a bargain purchase	413	-	-	**413**
Gain on sale of building	-	6,535	-	**6,535**
Other income	-	1,165	18	**1,183**
Operating expenses	(46,558)	(18,709)	(8,364)	**(73,631)**
Segment profit / (loss) before tax	17,193	7,728	(9,208)	**15,713**
Income tax (expense) / income	(4,832)	794	(160)	**(4,198)**
Segment profit / (loss) after tax	**12,361**	**8,522**	**(9,368)**	**11,515**
Loans and advances to customers	391,028	340,981	-	**732,009**
Other assets	134,865	278,692	(52,712)	**360,845**
Segment total assets	**525,893**	**619,673**	**(52,712)**	**1,092,854**
Customer deposits	(436,608)	(521,183)	-	**(957,791)**
Other liabilities	(26,915)	(71,437)	50,203	**(48,149)**
Segment total liabilities	**(463,523)**	**(592,620)**	**50,203**	**(1,005,940)**
Other segment items:				
Capital expenditure	(1,159)	(747)	(2)	**(1,908)**
Depreciation and amortisation	(3,103)	(702)	(13)	**(3,818)**

The "Group Centre" segment above includes the parent entity and all intercompany eliminations.

	Discontinued operations	Continuing operations					
Year ended 31 December 2012	Investment banking £000	Retail banking £000	UK Private banking £000	International private banking £000	Group Centre £000	**Total £000**	**Group Total £000**
Interest revenue	-	44,893	17,494	-	290	**62,677**	
Inter-segment revenue	-	(121)	(165)	-	(91)	**(377)**	
Interest revenue from external customers	-	44,772	17,329	-	199	**62,300**	
Fee and commission income	-	15,788	8,328	-	-	**24,116**	
Revenue from external customers	-	**60,560**	**25,657**	**-**	**199**	**86,416**	
Interest expense	-	(10,467)	(6,786)	(7)	209	**(17,051)**	
Subordinated loan note interest	-	-	-	-	(463)	**(463)**	
Fee and commission expense	-	(3,206)	(141)	-	-	**(3,347)**	
Segment operating income	-	47,008	18,895	(7)	(341)	**65,555**	
Gain from a bargain purchase	-	9,830	-	-	-	**9,830**	
Impairment losses	-	(8,946)	(2,038)	-	-	**(10,984)**	
Other income	-	37	-	334	25	**396**	
Gain on sale of subsidiary	-	-	-	-	839	**839**	
Operating expenses	**(383)**	(30,676)	(14,799)	(333)	(7,235)	**(53,043)**	
Segment profit / (loss) before tax	**(383)**	17,253	2,058	(6)	(6,712)	**12,593**	

Income tax (expense) / income	**36**	(1,591)	507	-	(44)	**(1,128)**	
Segment profit / (loss) after tax	**(347)**	**15,662**	**2,565**	**(6)**	**(6,756)**	**11,465**	**11,118**
Loans and advances to customers		297,631	289,337	-	-	**586,968**	**586,968**
Other assets		176,968	279,278	-	(43,205)	**413,041**	**413,041**
Segment total assets	**-**	**474,599**	**568,615**	**-**	**(43,205)**	**1,000,009**	**1,000,009**
Customer deposits		(398,891)	(495,654)	-	-	**(894,545)**	**(894,545)**
Other liabilities		(19,758)	(48,506)	-	31,448	**(36,816)**	**(36,816)**
Segment total liabilities	**-**	**(418,649)**	**(544,160)**	**-**	**31,448**	**(931,361)**	**(931,361)**
Other segment items:							
Capital expenditure	**-**	(810)	(17,451)	-	(13)	**(18,274)**	**(18,274)**
Depreciation and amortisation	**-**	(1,472)	(443)	-	(14)	**(1,929)**	**(1,929)**

Segment profit is shown prior to any intra-group eliminations.

The International private banking operations were in Switzerland. The UK private bank opened a branch in Dubai in the year, which generated £11k fee income and had operating costs of £890k. Other than the Switzerland operation that was sold in 2012 and the Dubai branch opened in 2013, all operations of the Group are conducted wholly within the United Kingdom and geographical information is therefore not presented.

44. Acquisition of V12 Finance Group Limited

On 2 January 2013 Secure Trust Bank acquired 100% of the ordinary share capital of V12 Finance Group Limited, which along with its wholly owned subsidiaries V12 Retail Finance Limited and V12 Personal Finance Limited provide retail loans, typically for 12 months on an unsecured basis to consumers who are predominantly classified as prime borrowers. The cash consideration for the companies of £3.5 million was paid on completion. The acquisition is complementary to the Group's existing retail finance proposition and the V12 management team will continue in the business.

As part of the acquisition Secure Trust Bank provided funding such that the V12 Finance Group could redeem £7.0 million of subordinated debt and repay existing bank finance amounting to £28.1 million.

The acquisition of V12 Finance Group Limited is accounted for in accordance with IFRS 3 'Business Combinations', which requires the recognition of the identifiable assets acquired and liabilities assumed at their acquisition date fair values. As part of this process, it is also necessary to identify and recognise certain assets and liabilities which are not included on the acquiree's balance sheet, for example intangible assets. The exercise to fair value the balance sheet is inherently subjective and required management to make a number of assumptions and estimates.

The Consolidated Statement of Comprehensive Income includes revenue of £5.1 million and a profit before tax of £0.5 million attributable to V12.

The following assets were acquired as part of the acquisition of the V12 Finance Group Limited and its wholly owned subsidiary entities:

	Acquired assets / liabilities £000	Fair value adjustments £000	Recognised values on acquisition £000
Cash	150	-	150
Loans and advances to customers	32,744	-	32,744
Other assets	619	-	619
Deferred tax assets	292	-	292
Intangible assets	17	5,443	5,460
Property, plant and equipment	176	-	176
Total assets	**33,998**	**5,443**	**39,441**
Loans and debt securities	35,076	-	35,076
Other liabilities	276	-	276

Deferred tax liability	34	1,252	1,286
Total liabilities	**35,386**	**1,252**	**36,638**
Net identifiable (liabilities)/assets	**(1,388)**	**4,191**	**2,803**
Consideration			3,507
Goodwill arising on acquisition			**704**

45. Ultimate controlling party

The Company regards Henry Angest, the Group Chairman and Chief Executive Officer, who has a beneficial interest in 53.7% of the issued share capital of the Company, as the ultimate controlling party. Details of his remuneration are given in the Remuneration Report and Note 41 of the consolidated financial statements includes related party transactions with Mr Angest.

46. Events after the balance sheet date

There were no material post balance sheet events.

Five Year Summary

In the table below, all the figures are presented in accordance with IFRS.

	2009 £000	2010 £000	2011 £000	2012 £000	2013 £000
Profit / (Loss) before tax *	5,050	5,104	5,116	12,593	15,713
Earnings per share					
Basic (p) **	23.4	25.0	(33.3)	52.6	51.9
Dividends per share (p)	22.0	23.0	24.0	25.0	44.0

Other KPIs:

	2009 £000	2010 £000	2011 £000	2012 £000	2013 £000
Earnings from continuing activities per share (p)	33.7	34.0	34.0	80.2	52.6
Net asset value per share (p)	227.6	227.7	312.2	449.3	570.5

* The profit before tax for 2011 is shown as the results of continuing operations. The previous years have not been restated but the contribution of the discontinued operation can be seen in the segmental analysis for those historical years.

** The earnings per share includes the effect of discontinued operations in 2011.